Supreme Court, U.S.
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No. 0

IN THE

Supreme Court of the United States

AMERICAN GENERAL LIFE INSURANCE COMPANY,

Petitioner,

v.

SPHERE DRAKE INSURANCE LIMITED,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

In the seminal case of *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145 (1968) – this Court's only decision addressing an arbitrator's disclosure obligation – the Court held that the failure of an arbitrator to disclose any non-trivial business relationship with the parties constitutes evident partiality and necessitates vacating an award under § 10(a)(2) of the Federal Arbitration Act (9 U.S.C. §§ 1 *et seq.*). In the parties' underlying arbitration, Sphere Drake's party-appointed arbitrator provided a false disclosure intended to mislead petitioner and the other two arbitrators into believing that he had no prior relationship with Sphere Drake. It was later discovered, after the panel issued a 2-to-1 award in Sphere Drake's favor (without discovery or a hearing), that he had acted as Sphere Drake's lawyer in a prior arbitration for which he personally billed over 379 hours. The district court, applying *Commonwealth Coatings*, vacated the award on grounds of evident partiality in light of the arbitrator's intentionally "misleading" and deficient disclosure. App. at 27a. The United States Court of Appeals for the Seventh Circuit reversed, fashioning a new rule directly in conflict with § 10(a)(2), *Commonwealth Coatings* and its progeny and disclosure rules promulgated by arbitration associations; the appellate court held that § 10(a)(2) applies only to the neutral arbitrator and not party-appointed arbitrators, despite the express language of the statute referring to "arbitrators" in the plural. Instead, the Seventh Circuit held that the arbitrator appointed by Sphere Drake owed no disclosure obligation in the first instance, even though (as expressly acknowledged by the appellate court) both sides intended that the two party-appointed arbitrators be "impartial adjudicators." App. at 5a.

The question presented is whether, in a tripartite arbitration, the parties and the third "neutral" arbitrator are entitled to receive full and candid disclosure from the party-appointed arbitrators at the outset of the proceeding concerning any prior non-trivial relationship with their nominating parties.

STATEMENT PURSUANT TO RULE 29.6

All American Life Insurance Company, appellee below, was merged into petitioner, American General Life Insurance Company, on December 31, 2002. American General Life Insurance Company is wholly owned by AGC Life Insurance Company, which is wholly owned by American General Corporation. American General Corporation's stock is owned by American International Group, Inc., which is a publicly held company (NYSE symbol, "AIG").

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Petitioner American General Life Insurance Company, formerly known as All American Life Insurance Company ("All American"), respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Seventh Circuit in this case.

OPINIONS BELOW

The decision of the district court granting petitioner's motion to vacate is reported at 2002 WL 1008464 (N.D. Ill. May 17, 2002). The decision of the court of appeals is reported at 307 F.3d 617 (7th Cir. 2002). Copies of these decisions are attached in the Appendix ("App.").

STATEMENT OF JURISDICTION

The court of appeals entered its judgment on October 9, 2002, App. at 1a, and denied a timely petition for rehearing *en banc* on November 4, 2002. App. at 39a. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

This case involves § 10(a)(2) of the Federal Arbitration Act, 9 U.S.C. §§ 1 *et seq.*, which provides, in relevant part:

> (a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration –
>
> . . .
>
> (2) where there was evident partiality or corruption in the arbitrators, or either of them.

STATEMENT OF THE CASE

Over the past decade, arbitration has gained wide acceptance in the business community as the preferred method of dispute resolution, greatly alleviating the burden imposed on court dockets throughout the country. Aided by a string of precedents from this Court beginning in the early 1980s, federal public policy favoring arbitration has been greatly strengthened. Parties view arbitration as an attractive alternative to litigation in large part because the Federal Arbitration Act, as enforced by this Court, provides safeguards to guarantee the integrity of the arbitral process – safeguards that are necessary given arbitrators' broad discretion to decide the law as well as the facts without any appellate review. Against this backdrop, the decision of the Seventh Circuit in this case – which upheld an arbitration award infected by an arbitrator's false and deceptive disclosure that he had no prior relationship with his appointing party when, in fact, he had represented that party as counsel in a prior arbitration – should not be allowed to stand. If parties who regularly use arbitration (including members of the reinsurance industry) are to have continued faith in the arbitral process, courts must vigilantly safeguard the integrity of the arbitral process, as this Court recognized decades ago in *Commonwealth Coatings*. Parties will cease including arbitration clauses in their contracts if they perceive that the process is unfair. The end result of the Seventh Circuit's decision upholding a tainted award and relieving party arbitrators of any disclosure obligation is *not* to promote arbitration, but rather to drive parties away from choosing arbitration as a viable means to obtain a just and fair resolution of their disputes.

A. Commencement Of The Underlying Arbitration

All American was an insurance company that had underwritten reinsurance for insurers issuing personal accident and occupational coverage directly to individuals and employers.[1] As part of those reinsurance underwriting activities, All American purchased its own reinsurance protection from other insurance companies, including respondent Sphere Drake Insurance Limited. In June 1999, All American commenced arbitration against Sphere Drake to obtain a declaration requiring Sphere Drake to honor its contractual obligations to provide reinsurance protection to All American under six reinsurance contracts in force between the parties. App. at 14a.

B. Disclosures By Sphere Drake's Party-Appointed Arbitrator

After the two party-appointed arbitrators and umpire were selected, the parties held an organizational meeting with the panel during which each panel member made a disclosure

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1. Reinsurance is the

> practice whereby primary insurers who have assumed risk from their policy holders in exchange for premiums, cede portions of that risk to reinsurers, in exchange for premiums, pursuant to reinsurance agreements. In turn, the reinsurers, often, cede portions of the assumed risk to their own reinsurers. In this way, the risk associated with any one policyholder is spread among a variety of insurers.
>
> *Stephens v. American Intern. Ins. Co.*, 66 F.3d 41, 42 (2d Cir. 1995).

concerning his current and past relationships with the parties, their respective law firms and the other panel members in accordance with the procedure agreed to among the panel and counsel. App. at 18a. For the purposes of this case, the only relevant disclosure was that made by Sphere Drake's party arbitrator – a disclosure that both the Seventh Circuit and the district court determined was false:

> With regard to the parties, this is the first contact that I've had with All American although I've known of the existence of the company obviously. In connection with Sphere Drake, I have known of Sphere Drake over the years and of Sphere Drake's parent Odyssey.

Id.

Based on the disclosures made during the organizational meeting, both sides agreed to certify the panel as duly constituted. *Id.*

By letter dated May 7, 2001, Sphere Drake's party arbitrator supplemented his disclosure and advised that he had neglected to mention his "limited" role in recommending his former law firm to serve as counsel to Sphere Drake's Bermuda subsidiary in an unrelated arbitration. App. at 19a.

Based on the limited scope of involvement by Sphere Drake's party arbitrator in a prior matter purportedly for a Bermuda subsidiary of Sphere Drake (not Sphere Drake itself), All American had no reason to be concerned about the supplemental disclosure or to suspect any prior attorney-client relationship between Sphere Drake and its party arbitrator. Sphere Drake's party arbitrator made no further disclosure concerning his prior relationship with Sphere Drake.

C. The Arbitration Panel Majority's Award

At the organizational meeting, Sphere Drake requested permission to file a "Motion for Judgment on the Pleadings" seeking dismissal of All American's claims prior to conducting discovery or submitting evidence. App. at 19a. The panel agreed to entertain the motion over All American's objection. *Id.* On July 5, 2001, a majority of the panel, with All American's party arbitrator in dissent, issued a final award granting Sphere Drake's Motion for Judgment on the Pleadings and dismissing the arbitration, with prejudice and on the merits. App. at 20a.

D. The Decisions Below

In discovery taken during post-award proceedings in this case, All American obtained evidence demonstrating that Sphere Drake's party arbitrator had a prior significant, undisclosed attorney-client relationship with Sphere Drake. First, the prior arbitration that was referenced in the supplemental disclosure letter was against Sphere Drake, not Sphere Drake's Bermuda subsidiary. App. at 22a. Second, Sphere Drake's party arbitrator played a far greater role in the prior arbitration than simply providing the "limited corporate advice" of recommending his "former" firm – he was counsel of record for Sphere Drake in the prior arbitration, billing 379.35 hours on the matter and generating $132,737.50 in legal fees. App. at 23a. Third, Sphere Drake's party arbitrator failed to disclose that he worked on another prior arbitration for Sphere Drake and two other matters for Sphere Drake's Bermuda subsidiary, resulting in more than 60 billable hours and amounting to $22,575 in legal fees. *Id.*

Based on these facts, All American moved to vacate the award, claiming, *inter alia*, that the affirmatively false and misleading disclosures made by Sphere Drake's party arbitrator at the organizational meeting and in the supplemental disclosure letter demonstrated evident partiality under § 10(a)(2) of the FAA.

The district court granted All American's cross-motion to vacate based on a finding that Sphere Drake's party arbitrator was evidently partial due to his failure to disclose a substantial four-year attorney-client relationship with Sphere Drake. App. at 29a. In particular, the court found the supplemental disclosure letter affirmatively "misleading" because the purported "limited corporate advice" in fact amounted to "more than four hundred hours of work performed over four years." App. at 27a-28a. The district court also found the arbitrator's assertion that he represented only the Bermuda subsidiary of Sphere Drake in a prior arbitration "plainly inaccurate." *Id.* at 28a. He was "counsel of record for Sphere Drake itself" in the prior arbitration and (contrary to the arbitrator's representation) it was Sphere Drake, not the Bermuda subsidiary, which was "the named reinsurer on the contract in dispute." *Id.* The district court characterized the arbitrator's inadequate disclosure as "negligent or even intentional" and noted that the "court is unaware of any case where an arbitrator has offered such an ineffective description of his connection to a party." App. at 30a.

On Sphere Drake's appeal, the Seventh Circuit reversed the district court in an opinion that disregards the plain language of § 10(a)(2) of the FAA, and squarely conflicts with this Court's holding in *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145 (1968). Sustaining

an unprecedented argument that Sphere Drake advanced for the first time on appeal, the Seventh Circuit held that a party-appointed arbitrator in a tripartite arbitration owes no disclosure obligation, even if (as here) both sides intended that the party arbitrators be "impartial adjudicators." App. at 5a. The only relevant question, according to the court of appeals, is whether the party arbitrator's prior relationship with the appointing party would be sufficient to disqualify the arbitrator if he were a judge presiding over the dispute in court. App. at 7a ("If [the arbitrator] could have served as a federal judge in this case, it is impossible to see how his background could demonstrate 'evident partiality' within the meaning of § 10(a)(2)."). The court ignored the fact that Sphere Drake's party arbitrator not only failed to disclose his substantial attorney-client relationship with the appointing party, but also purposefully concealed this relationship from All American and the other arbitrators; the deception by Sphere Drake's party arbitrator rendered it impossible for All American to make an informed evaluation of the arbitrator's ability to serve and the umpire to make an informed judgment about the proper weight to accord the arbitrator's views in deliberations. In a striking departure from this Court's precedent, the Seventh Circuit adopted a disclosure standard that permits a party-appointed arbitrator to unilaterally determine whether he has a disabling conflict and to withhold from his fellow arbitrators and opposing counsel matters affecting an evaluation of his credibility and potential bias.

This Petition for a Writ of Certiorari followed.

REASONS FOR GRANTING THE PETITION

The Seventh Circuit's holding directly conflicts with this Court's seminal pronouncement in *Commonwealth Coatings* that all arbitrators are required to disclose any relationship with the parties that is "more than [a] trivial business" relationship. *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145, 151-52 (1968) (White, J., concurring); *see also id.* at 149 (arbitrators are required to "disclose to the parties any dealings that might create an impression of possible bias") (Black, J., plurality).[2] Absent such a rule, neither the parties nor the other arbitrators can make an informed evaluation of the party arbitrator's partiality. Rather than establishing an "atmosphere of frankness" necessary to maintain confidence in the integrity

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2. There is a circuit split regarding which of the two tests in *Commonwealth Coatings* is applicable. Some circuits apply the test set forth in Justice White's concurring opinion, while others use the test established in Justice Black's plurality decision or some variation thereof. *Compare ANR Coal Co., Inc. v. Cogentrix of North Carolina*, 173 F. 3d 493, 499 n.3 (4th Cir. 1999) (noting that courts have given particular weight to Justice White's concurrence); *Merit Ins. Co. v. Leatherby Ins. Co.*, 714 F.2d 673, 682 (7th Cir. 1983) (treating Justice White's opinion as "authoritative") (citing *United States Wrestling Fed'n v. Wrestling Div. of AAU, Inc.*, 605 F.2d 313, 319 (7th Cir. 1979)) *with Schmitz v. Zilveti*, 20 F.3d 1043, 1048 (9th Cir. 1994) (holding that the "best expression" of the Supreme Court's decision was that evident partiality was present when "undisclosed facts show a reasonable impression of partiality."); *University Commons-Urbana, Ltd. v. Universal Constructors Inc.*, 304 F.3d 1331, 1338 (11th Cir. 2002) (an arbitrator is obligated to disclose those facts that "'create a reasonable impression of bias.'"). Under either standard, however, an arbitrator's substantial four-year attorney-client relationship with the party that appointed him is the type of relationship that should have been disclosed.

of the arbitration process, *id.* at 151 (White, J., concurring), the Seventh Circuit's decision encourages deception by party arbitrators in disclosing their prior relationships with the parties since the act of concealing one's prior relationship creates no inference of partiality under the court's analysis. Indeed, under the appellate court's ruling, a party arbitrator would correctly conclude that he is better off making a false disclosure in the hope that his prior relationship will go undetected, rather than making a truthful disclosure at the outset and risk facing a likely challenge to his appointment.

Allowing such a holding to stand would seriously undermine efforts to promote arbitration as a fair and efficient alternative to litigation, frustrating the strong public policy underlying the FAA and the decisions of this Court favoring arbitration as a dispute resolution mechanism.

POINT I

THE DISCLOSURE RULE ADOPTED IN *COMMONWEALTH COATINGS* APPLIES TO PARTY-APPOINTED ARBITRATORS

A. The Seventh Circuit's Decision Is Contrary To § 10(a)(2) Of The FAA And *Commonwealth Coatings*

The Seventh Circuit construed the *Commonwealth Coatings* disclosure requirement to apply only to a neutral arbitrator (or umpire) in a tripartite arbitration, and not to party-appointed arbitrators. This narrow interpretation conflicts with the plain language of § 10(a)(2) of the FAA and *Commonwealth Coatings* and its progeny.

Section 10 of the FAA authorizes a district court to vacate an arbitration award where there was "evident partiality or corruption in the arbitrators, *or either of them*." 9 U.S.C. § 10(a)(2) (emphasis added). By referring to "arbitrators" in the plural and adding the phrase "or either of them," Congress manifested its intent that this statutory ground for vacating an award apply to all three arbitrators of a tripartite panel. *See Standard Tankers (Bahamas) Company, Ltd. v. Motor Tank Vessel, Akti*, 438 F. Supp. 153, 159 (E.D.N.C. 1977) (the language of the statute "directs that the evident partiality test should apply to *every member of the panel*," including the party-appointed member) (emphasis added); *see also* Doak Bishop & Lucy Reed, *Practical Guidelines for Interviewing, Selecting and Challenging Party-Appointed Arbitrators in International Commercial Arbitration*, 14 Arb. Int'l 395, 403 (1998) (the FAA "makes no clear distinction between party-appointed arbitrators and sole or presiding arbitrators. . . . The reference to 'the arbitrators, or either of them' is an indication that none of the arbitrators is permitted to be partial."); James H. Carter, *Living with the Party-Appointed Arbitrator: Judicial Confusion, Ethical Code and Practical Advice*, 3 Am. Rev. Int'l Arb. 153, 158-159 (1992) ("Whether an arbitrator on a tripartite tribunal is party-appointed or chosen by the party-appointed arbitrators as their chairman, the statutory language [of § 10 of the FAA] suggests that he or she is required to be impartial unless the parties expressly agree otherwise."). If Congress had intended to limit the scope of § 10, it would have referred to evident partiality or corruption "in the sole or neutral arbitrator" (or other words to that effect).

Moreover, the decision in *Commonwealth Coatings*, this Court's only decision addressing an arbitrator's duty of disclosure, leaves no doubt that the Court's disclosure

requirement applies to all three arbitrators on a tripartite panel:

> The arbitration process functions best when an amicable and trusting atmosphere is preserved and there is voluntary compliance with the decree, without need for judicial enforcement. This end is best served by establishing an atmosphere of frankness at the outset, through disclosure by the arbitrator of *any* financial transactions which he has had or is negotiating with either of the parties. . . . Of course, an arbitrator's business relationships may be diverse indeed, involving more or less remote commercial connections with great numbers of people. He cannot be expected to provide the parties with his complete and unexpurgated business biography. *But it is enough for present purposes to hold, as the Court does, that where the arbitrator has a substantial interest in a firm which has done more than trivial business with a party, that fact must be disclosed.*

Commonwealth Coatings, 393 U.S. at 151-52 (White, J., concurring) (emphasis added). There can be no "atmosphere of frankness" where only one of three arbitrators on a tripartite panel is required to disclose his or her prior relationships with the parties and the other two are not.

Similarly, Justice Black's plurality opinion in *Commonwealth Coatings* draws no distinction between neutral arbitrators and party-appointed arbitrators. Justice Black held that § 10 of the FAA demonstrates "a desire of Congress to provide not merely for any arbitration but for an

impartial one." 393 U.S. at 147. Justice Black used broad language to describe the Court's disclosure rule:

> We can perceive no way in which the effectiveness of the arbitration process will be hampered by the simple requirement that *arbitrators* disclose to the parties any dealings that might create an impression of possible bias.

Id. at 149 (emphasis added). Of course, the opinions of both Justice Black and Justice White implicitly require that the disclosures be accurate and truthful.

The *Commonwealth Coatings* case involved precisely the same type of tripartite panel as this case – two party-appointed arbitrators and an umpire. *Id.* at 146. If the Court meant to limit the application of its disclosure rule to only the umpire, surely it would have said so. Instead, the Court described the disclosure requirement as applying to "arbitrators," without distinction. *See Standard Tankers*, 438 F. Supp. at 159 (rejecting party's argument that *Commonwealth Coatings* applied only in cases involving the third or neutral arbitrator, reasoning that "neither the lead nor concurring opinion delimits the holding in such a manner.").[3]

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3. Notably, the Supreme Court in *Commonwealth Coatings* adopted its *per se* prophylactic disclosure rule even though: (1) the arbitrator was "not asked about [his] business connections with either party" and was "innocent of any . . . improper motive"; (2) petitioner's counsel "candidly admitted that if he had been told about the arbitrator's prior relationship" he would not have objected to the arbitrator; and (3) the award was unanimous. 393 U.S. at 152-53 (Fortas, J., dissenting).

The Seventh Circuit's misguided holding that the prophylactic rule announced in *Commonwealth Coatings* does not apply to party-appointed arbitrators stems, at least in part, from the court's implicit finding that disclosure by a party arbitrator serves no salutary purpose if the facts to be disclosed would not result in the arbitrator's disqualification. However, disclosure by a party-appointed arbitrator provides the umpire with information that is necessary to assess the appropriate weight to be given to the party-appointed arbitrator's views. *See* Stephen C. Rogers, *Can Tripartite Arbitration Panels Reach Fair Results?*, 8 No. 1 Disp. Resol. Mag. 27, 29 (Fall 2001) ("What the neutral learns about the party arbitrators' relationships with their parties should also be useful to him in evaluating the points those arbitrators make to him about the case.").

The Seventh Circuit, without explanation or record support, determined that the false and misleading disclosure by Sphere Drake's party arbitrator had no adverse impact on the umpire's ability to assess the credibility of the positions advanced by that arbitrator in deliberations. App. at 11a ("[W]e have not been given any reason to think that [the umpire] wanted more information from [Sphere Drake's party arbitrator] in order to know what to make of [his] arguments during the panel's deliberations"). Common sense suggests that an umpire would want to know that a party arbitrator had a sustained and significant attorney-client relationship with the appointing party in assessing his position and potential bias during deliberations. It is for this reason that the Seventh Circuit's failure to find purpose in any disclosure beyond that required by a judge presiding over a lawsuit is fundamentally flawed.

B. The Seventh Circuit's Decision Directly Conflicts With Decisions From Other Jurisdictions, The Parties' Agreement And The Clear Preference Among Arbitration Associations In Favor Of Full And Candid Disclosure By Party-Appointed Arbitrators

The Seventh Circuit's erroneous interpretation of *Commonwealth Coatings* squarely conflicts with decisions from other courts applying the disclosure requirement of *Commonwealth Coatings* to all arbitrators – including party-appointed arbitrators. *See Metropolitan Prop. & Cas. Ins. Co. v. J.C. Penney Cas. Ins. Co.*, 780 F. Supp. 885, 893 (D. Conn. 1991) (party-appointed arbitrator "must disclose at the time of his appointment 'any circumstances likely to create a presumption of bias or which he believes might disqualify him as an impartial Arbitrator.'") (citing *Commonwealth Coatings*, 393 U.S. at 149); *Barcon Assoc., Inc. v. Tri-County Asphalt Corp.*, 430 A.2d 214, 215-16 (N.J. 1981) ("[E]very arbitrator, whether party-designated or 'neutral,' [must] disclose to the parties, prior to the commencement of arbitration proceedings, any relationship or transaction that he has had with the parties or their representatives."); *Northwest Mech., Inc. v. Public Utils. Comm'n of the City of Virginia*, 283 N.W.2d 522, 523 (Minn. 1979) (applying the *Commonwealth Coatings* disclosure requirement to both a party-designated arbitrator and a neutral arbitrator). *Cf. Florasynth, Inc. v. Pickholz*, 750 F.2d 171, 173 (2d Cir. 1984) ("Although the panel was made up of two arbitrators appointed by the parties and one 'neutral' arbitrator, *there is no question that all three members of the panel have a responsibility to be disinterested.*") (emphasis added).

For example, in *Metropolitan Property*, the court found that a party-appointed arbitrator exhibited evident partiality

by, *inter alia*, failing to disclose certain *ex parte* communications with his nominating party which took place prior to his appointment. While recognizing that party selected arbitrators are not expected to be "neutral," the *Metropolitan Property* court nevertheless concluded that this "does not mean that such arbitrators are excused from their ethical duties and the obligation to participate in the arbitration process in a fair, honest and good-faith manner." *Metropolitan Prop.*, 780 F. Supp. at 890-92. Part of this obligation includes the duty to disclose "any circumstances likely to create a presumption of bias." *Id.* at 893 (citing *Commonwealth Coatings*, 393 U.S. at 149). Similarly, the court in *Barcon* vacated an arbitration award due to the failure of one of the party appointed arbitrators to disclose a substantial commercial relationship with his nominating party. The court in *Barcon* explained that a "party can make a sound judgment as to an arbitrator's possible partiality only if the arbitrator discloses all relevant information." *Barcon Assoc., Inc.*, 430 A.2d at 222. Therefore, the court concluded, every arbitrator, neutral or party-designated, must disclose "any dealings that might create an impression of possible bias." *Id.* at 220 (citing *Commonwealth Coatings*, 393 U.S. at 149).

The Seventh Circuit's decision also squarely conflicts with the parties' agreement. The court of appeals observed that parties may agree in their arbitration clause to allow party-appointed arbitrators to be partial, and by doing so waive their right to invoke § 10(a)(2) to challenge any award on the grounds of evident partiality with respect to the party arbitrators. App. at 5a ("To the extent that an agreement entitles parties to select interested (even beholden) arbitrators, § 10(a)(2) has no role to play."). Such a contractual waiver is, in fact, what occurred in the *Delta Mine* case, where both

sides agreed that party-appointed arbitrators could be current employees or counsel of the parties. *Delta Mine Holding Co. v. AFC Coal Properties, Inc.*, 280 F.3d 815, 817 (8th Cir. 2002). By contrast, All American and Sphere Drake in this case specifically agreed (as acknowledged by the Seventh Circuit) that the party-appointed arbitrators were intended to be "impartial adjudicators." App. at 5a. In the absence of a waiver by All American of its right to invoke § 10(a)(2), the disclosure requirement set forth in *Commonwealth Coatings* and its progeny should have applied to Sphere Drake's party-appointed arbitrator.

Finally, the need for full disclosure from all arbitrators is clearly reflected in the various sets of rules available in both domestic and international arbitrations, which impose a uniform disclosure standard on party-appointed and neutral arbitrators alike. For example, the AIDA Reinsurance and Insurance Society ("ARIAS-U.S."),[4] the insurance arbitration society under whose auspices the Seventh Circuit found the parties' arbitration had been conducted, subjects all three arbitrators on a tripartite panel to the same disclosure obligation. App. at 2a. The preamble to the ARIAS-U.S. Code of Conduct expressly states that "[u]nless inconsistent with the agreement of the parties or applicable law, *the two arbitrators appointed by the parties* should observe the same ethical standards as a single arbitrator or an umpire on a panel of arbitrators" with respect to disclosure. ARIAS-U.S., Code of Conduct, *available at* http://www.arias-us.org/arb_and_ump/purpose.shtml (emphasis added). The

4. ARIAS-U.S. is an organization formed to promote the improvement of the insurance/reinsurance arbitration process and to provide the training necessary to serve effectively on an insurance/reinsurance panel. App. at 15a n.1. Sphere Drake's party arbitrator was a founding director of ARIAS-U.S. App. at 15a.

comment to Canon IV of the ARIAS-U.S. Code of Conduct, which addresses the disclosure obligations of arbitrators, draws *no distinction* between party-appointed arbitrators and umpires. Likewise, Chapter 3 of the ARIAS-U.S. Practical Guide recognizes that all arbitrators should offer full and complete disclosure at the outset of the arbitral process:

> At the Organizational Meeting, *all members of the panel* should reveal on the record their past, present and any known future business and personal relationships with the parties, the parties' counsel, other panel members, and potential witnesses who are identified in documents provided to the panel members.

ARIAS-U.S. Practical Guide, *available at* http://www.arias-us.org/res_and_pro/chapter03.shtml (emphasis added).

In addition, the American Bar Association has undertaken an effort to revise the Code of Ethics for Arbitrators so that the disclosure obligations of party-appointed arbitrators parallel those of neutral arbitrators. The current code, adopted in 1977, provides that disclosure by non-neutral arbitrators "need not include as detailed information as is expected from persons appointed as neutral arbitrators." American Bar Association Code of Ethics for Arbitrators in Commercial Disputes, Canon VII. However, the 2000 Revision of the Code, which was prepared by a committee comprised of representatives from the ABA, the AAA and the CPR Institute for Dispute Resolution, eliminates any language suggesting a less stringent disclosure standard for non-neutrals. *See Code of Ethics for Arbitrators in Commercial Disputes (Proposed Revision 2000)*, 671 PLI/Lit 1039, * 1056 (March 2002). Rather, the revised Code provides that party-appointed

arbitrators are required to "disclose to all parties and to the other arbitrators all interests and relationships" that the umpire must disclose, which includes "any known existing or past financial, business, [or] professional, . . . relationship which are likely to affect impartiality or which might reasonably create an appearance of partiality or bias." *Id.* at 1056 and 1048.

Similarly, the requirement of complete disclosure by all arbitrators has been recognized by organizations governing the activities of international arbitrations. *See* UNCITRAL Arbitration Rules Article 9 ("A prospective arbitrator shall disclose to those who approach him in connexion [sic] with his possible appointment any circumstances likely to give rise to justifiable doubts as to his impartiality or independence."); AAA International Rules Article 7(1) ("Prior to accepting appointment, a prospective arbitrator shall disclose to the administrator any circumstances likely to give rise to justifiable doubts as to the arbitrator's impartiality or independence."); ICC Rules of Arbitration Article 7(2) ("Before appointment or confirmation, a prospective arbitrator shall sign a statement of independence and disclose in writing . . . any facts or circumstances which might be of such a nature as to call into question the arbitrator's independence in the eyes of the parties."); *see also* James H. Carter, *Improving Life with the Party-Appointed Arbitrator: Clearer Conduct Rules for "Nonneutrals,"* 11 Am. Rev. Int'l Arb. 295, * 296 (2000) ("The 'international' view is that all arbitrators, including party-appointed arbitrators, generally are held to similar disclosure and disqualification standards and that disclosure failures by any arbitrator may provide a basis for setting aside an award."); Bishop & Reed, *supra*, at 397-98 ("All of the major private international arbitration rules contain some

variation of the most fundamental standards for the qualification and conduct of arbitrators: impartiality and independence.").

Hence, the Seventh Circuit's decision exempting party-appointed arbitrators from the *Commonwealth Coatings* disclosure obligations, even where (as here) the parties agreed that all three arbitrators would be "impartial adjudicators," is directly contrary to the practice both in domestic and international arbitrations of requiring full and complete disclosure by all arbitrators (not just the umpire) in order to promote and maintain the integrity of the arbitral process.

POINT II

FAILURE TO REQUIRE FULL AND HONEST DISCLOSURE FROM ALL ARBITRATORS WILL UNDERMINE THIS COURT'S DECISIONS ENCOURAGING ARBITRATION AS AN ALTERNATIVE TO LITIGATION

The practice of requiring full and candid disclosure by all arbitrators will help promote arbitration as a viable and attractive alternative to litigation. Prior to the enactment of the FAA in 1925, the federal courts tended to view the practice of arbitration as a potentially dangerous threat to their own jurisdiction and therefore often refused to enforce arbitration agreements; the FAA was passed in large part to "reverse the longstanding judicial hostility to arbitration agreements that had existed at English common law and had been adopted by American courts, and to place arbitration on the same footing as other contracts." *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24 (1991). The skepticism with which courts viewed arbitration progressively abated throughout the

twentieth century, and it is evident from more recent precedent that the federal judiciary now uniformly views arbitration as a welcome substitute for traditional litigation. *See Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626-27 (1985) ("[W]e are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration as an alternative means of dispute resolution.").

This change in attitude toward the practice of arbitration is clearly visible in this Court's recent jurisprudence on the subject of arbitration. Beginning in the early 1980's and continuing through the current term, this Court has decided a number of significant cases under the FAA that promote the "liberal federal policy favoring arbitration agreements."[5] *Moses H. Cone Memorial Hospital v. Mercury Const. Corp.*, 460 U.S. 1, 24 (1983).

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5. The Court's embrace of arbitration in recent years has been the subject of significant scholarly commentary. *See, e.g.*, Jonathan Boonin & James L. Stone, *The Supreme Court's Emerging Endorsement of Arbitration*, 30-SEP Colo. Law. 67, * 68 (Sept. 2001) (describing this Court's recent arbitration jurisprudence as demonstrating "a continuing, evolving, and wide-ranging endorsement of arbitration as a viable form of dispute resolution."); Richard H. Kreindler, *Arbitration: A Creative Alternative to Intellectual Property Litigation In Light of Two Recent U.S. Supreme Court Decisions*, 9 World Arb. & Mediation Rep. 13 (Jan. 1998) ("[T]he comparison of arbitration and litigation in the context of arbitrability or justiciability has evolved dramatically in favor of arbitration."); Stephen L. Hayford, *Commercial Arbitration in the Supreme Court 1983-1985: A Sea Change*, 31 Wake Forest L. Rev. 1, * 1 (Spring 1996) ("During the past decade, the Supreme Court resoundingly endorsed the emergence of arbitration as a primary forum for the resolution of commercial disputes.").

For example, this Court has decided cases that have: (1) expanded the scope of arbitrable issues under the FAA, *Gilmer v. Interstate/Johnson Lane Corp*, 500 U.S. 20 (1991) (age discrimination claims), *De Quijas v. Shearson/American Express Inc.*, 490 U.S. 477 (1989) (securities claims), *Mitsubishi Motors*, 473 U.S. at 614 (antitrust claims); (2) provided arbitrators greater authority to fashion remedies, such as awarding punitive damages, *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52 (1995); (3) upheld the use of arbitration agreements in contracts of employment, *Circuit City Stores v. Adams*, 122 S. Ct. 2329 (2002); and (4) empowered arbitrators to determine potentially dispositive threshold issues, *Howsam v. Dean Witter Reynolds, Inc.*, 123 S. Ct. 588 (2002). Taken together, these cases have considerably increased both the power vested in arbitrators and the range of disputes that are subject to arbitration. At the same time, the increasing expenses of traditional litigation coupled with the substantial backlogs common in both federal and state courts has led to a steady rise in the number of litigants opting to use arbitration as a means of resolving their disputes. *See* Roy Israel, *The Role of Arbitration*, 5/98 Metro. Corp. Couns. 41 (May 1998) (citing a study revealing that 79 percent of 1,000 of the largest U.S. corporations had used arbitration between 1995 and 1998 and reporting that in 1996, more than 100,000 cases were filed with ADR providers representing cases in an assortment of industries including commercial finance, health care, real estate, insurance and employment); Catherine Cronin-Harris, *Mainstreaming: Systematizing Corporate Use of ADR*, 59 Alb. L. Rev. 847, * 858 (1996) (citing a 1994 survey of 124 major corporate law firms in which 80 percent claimed that client interest in alternative dispute resolution had increased over the prior three years).

It is now imperative that, in light of the evolution in the practice of arbitration that has occurred since 1968 (when *Commonwealth Coatings* was decided), this Court reaffirm that the rule announced in *Commonwealth Coatings* applies to all arbitrators, whether party-appointed or neutral. This is necessary both to ensure that arbitrators do not abuse their broad procedural and substantive authority and to prevent the Seventh Circuit's decision in this case from undermining the public's confidence in arbitration as a fair and just alternative to litigation.

A. Strict Disclosure Standards Are A Necessary Check On The Significant Power Exercised By Arbitrators

In light of the amount of authority ceded to arbitrators under the FAA and this Court's jurisprudence, it is critical that § 10(a)(2) be applied as intended, *i.e.*, "stringently." *University Commons-Urbana, Ltd. v. Universal Constructors Inc.*, 304 F.3d 1331, 1338 (11th Cir. 2002). As the *Commonwealth Coatings* plurality stated:

> [W]e should, if anything, be even more scrupulous to safeguard the impartiality of arbitrators than judges, since the former have completely free rein to decide the law as well as the facts and are not subject to appellate review.

393 U.S. at 149.

The Seventh Circuit itself recognized that industry arbitration "often uses panels composed of industry insiders, the better to understand the trade's norms of doing business and the consequences of proposed lines of decision." App. at 4a. Thus, whereas a judge makes a conscious decision

to leave the world of business affairs in order to become a member of the judiciary, an arbitrator is generally chosen for the very fact that he remains part of the business community. This reality and the resulting need to assess potential bias demand that the parties and other arbitrators be cognizant of the extent of an arbitrator's relationship to the party that selected him or her, which can only be achieved through the full and candid disclosure required by this Court in *Commonwealth Coatings*.

The acknowledgment that arbitrators cannot, and should not, be expected to be as impartial as judges does not require turning a blind eye to deception by an arbitrator who intentionally provides a misleading disclosure of his prior relationship with one of the parties:

> This [distinction between judges and arbitrators] does not mean the judiciary must overlook outright chicanery in giving effect to their awards; that would be an abdication of our responsibility.

Commonwealth Coatings, 393 U.S. at 150 (White, J. concurring); *see also Astoria Med. Group v. Health Ins. Plan of Greater New York*, 11 N.Y.2d 128, 137 (N.Y. 1962) (stating in reference to a party-appointed arbitrator: "[p]artisan he may be, but not dishonest."). Indeed, even the dissenting opinion in *Commonwealth Coatings*, in arguing in favor of confirming the award, took pains to distinguish the circumstance where (as here) an arbitrator intentionally makes a false and misleading disclosure:

> Both courts below held, and petitioner concedes, that the third arbitrator was innocent of any actual partiality, or bias, or improper motive. *There is*

> *no suggestion of concealment as distinguished from the innocent failure to volunteer information.*

393 U.S. at 152 (Fortas, J., dissenting) (emphasis added).

The Seventh Circuit "abdicated its responsibility" by condoning the false and misleading disclosure provided by Sphere Drake's party arbitrator, while seriously impacting the internal dynamics of tripartite panels and undermining the integrity of the arbitral process itself.

B. Allowing Party-Appointed Arbitrators To Provide Incomplete or Misleading Disclosure Will Erode The Public's Confidence In Arbitration

The Seventh Circuit's holding that a party arbitrator intended to be an "impartial adjudicator" (App. at 5a) may provide intentionally deceptive information in the disclosure process without consequence seriously undermines the objective of § 10(a)(2), which is to maintain the integrity of the arbitral process. *See Barcon Assoc., Inc. v. Tri-County Asphalt Corp.*, 430 A.2d 214, 219-20 (N.J. 1981) ("[A] party-designated arbitrator . . . must remain faithful to the obligation which rests upon him to maintain 'broad public confidence in the integrity and fairness of the (arbitration) process.'") (citing to the First Code of Ethics for Arbitrators in Commercial Disputes jointly drafted by the American Arbitration Association and the American Bar Association); *Metropolitan Prop. & Cas. Ins. Co. v. J.C. Penney Cas. Ins. Co.*, 780 F. Supp. 885, 893 (D. Conn. 1991) ("[E]ven a party-appointed arbitrator in the tripartite context 'has a responsibility not only to the parties but also to the process itself, and must observe high standards of conduct so that the integrity and fairness of the process will be preserved.'");

Aetna Cas. & Sur. Co. v. Grabbert, 590 A.2d 88, 92 (R.I. 1991) ("As a general rule we feel that no matter how desirable the finality of an arbitration award may be, it is more important that an award be rendered free from any improprieties that affect the award and that could destroy public confidence in and the integrity of the arbitration process.").

Allowing an award to stand where an arbitrator intentionally provides a false and misleading disclosure will erode the public's confidence in the integrity of the arbitral process, and thereby undermine the federal policy favoring arbitration. First, party arbitrators, newly aware that they may conceal their prior relationships during the disclosure process without jeopardizing an award, will err on the side of nondisclosure to avoid potential disqualification motions. The new rule for party arbitrators will be "the less said the better." Second, parties who are regular participants in tripartite arbitrations and umpires on tripartite panels will have no reason to trust that disclosures made by party arbitrators will be truthful, thereby eroding the "atmosphere of frankness" viewed as necessary by the Court in *Commonwealth Coatings* to the proper functioning of the arbitral process. 393 U.S. at 151.

CONCLUSION

For the reasons set forth above, the Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX

APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT DATED AND DECIDED OCTOBER 9, 2002

In the
UNITED STATES COURT OF APPEALS
For the Seventh Circuit

No. 02-2458

SPHERE DRAKE INSURANCE LIMITED,

Plaintiff-Appellant,

v.

ALL AMERICAN LIFE INSURANCE COMPANY,

Defendant-Appellee.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.
No. 01 C 5226—**Rebecca R. Pallmeyer**, *Judge.*

ARGUED SEPTEMBER 9, 2002—DECIDED OCTOBER 9, 2002

Before EASTERBROOK, KANNE, and EVANS, *Circuit Judges.*

EASTERBROOK, *Circuit Judge.* Two underwriters cannot agree about whether seven policies of reinsurance are valid —or for that matter about who decides whether they are valid. All American, which contends that the contracts are

effective, says that the dispute should be arbitrated. Sphere Drake, which denies the documents' binding quality, believes that a court should resolve the question. Last year we concluded that disputes about one of the seven contracts should be handled by a judge. Euro International Underwriting ("EIU"), which wrote the policies on Sphere Drake's behalf, was subject to a cap on the risks to which it could expose Sphere Drake. According to Sphere Drake, EIU exceeded this limit when agreeing to reinsure All American's policies. If that is so true, and All American (or its agent) knew it, then EIU had neither actual nor apparent authority to bind Sphere Drake, which would not be obliged either to arbitrate or to indemnify. See *Sphere Drake Insurance Ltd. v. All American Insurance Co.*, 256 F.3d 587 (7th Cir. 2001).

While litigating with respect to one of the seven policies, Sphere Drake submitted the other six to arbitration at All American's insistence. The arbitration was conducted under the auspices of the Association Internationale de Droits des Assurances ("AIDA") and its U.S. affiliate, the AIDA Reinsurance and Insurance Arbitration Society ("ARIAS•U.S."), which uses tripartite panels. Each insurer names one member of the panel, and these two choose a neutral (called the "umpire") to break ties. All American designated Robert M. Mangino, and Sphere Drake named Ronald A. Jacks. They chose Robert M. Huggins as the umpire. All three have considerable experience in international reinsurance arbitration, having served on at least 35 panels. Mangino and Jacks are founding directors of ARIAS•U.S.; Jacks is a former president of the U.S. chapter of AIDA. All three have served as umpires; Jacks has been

chosen for that duty more than 25 times by party-named arbitrators who relied on his reputation for legal acumen and impartiality. Huggins decided that Sphere Drake was entitled to victory on the ground that All American had disavowed Stirling Cooke Brown Reinsurance Brokers as its agent (a tactic apparently designed to avoid any risk that Stirling Cooke, which placed the reinsurance through EIU, would be found to know about EIU's limited authority). But Huggins concluded that if All American was not bound (because Stirling Cooke lacked authority to act on its behalf) then Sphere Drake could not be bound either. Jacks joined him to make a majority; Mangino dissented. Having demanded arbitration, All American decided that it did not like the result and asked a court to set aside the award—which it did, on the ground that Jacks displayed "evident partiality," one of the few grounds for refusing to enforce an award. 9 U.S.C. §10(a)(2). See 2002 U.S. Dist. LEXIS 8876 (N.D. Ill. May 17, 2002).

As far as we can see, this is the first time since the Federal Arbitration Act was enacted in 1925 that a federal court has set aside an award because a party-appointed arbitrator on a tripartite panel, as opposed to a neutral, displayed "evident partiality." The lack of precedent is unsurprising, because in the main party-appointed arbitrators are *supposed* to be advocates. In labor arbitration a union may name as its arbitrator the business manager of the local union, and the employer its vice-president for labor relations. Yet no one believes that the predictable loyalty of these designees spoils the award. See *Astoria Medical Group v. Health Insurance Plan of Greater New York*, 227 N.Y.S.2d 401, 182 N.E.2d

85 (1962). Cf. *United Transportation Union v. Gateway Western Ry.*, 284 F.3d 710 (7th Cir. 2002) (discussing the difference between party-appointed and neutral arbitrators). This is so because the parties are entitled to waive the protection of §10(a)(2), as they can waive almost any other statutory entitlement. See *Evans v. Jeff D.*, 475 U.S. 717 (1986); *United States v. Krilich*, 159 F.3d 1020 (7th Cir. 1998) (collecting authority). The Federal Arbitration Act makes arbitration agreements enforceable to the same extent as other contracts, so courts must "enforce privately negotiated agreements to arbitrate, like other contracts, in accordance with their terms." *Volt Information Sciences, Inc. v. Stanford University*, 489 U.S. 468, 478 (1989).

Parties are free to choose for themselves to what lengths they will go in quest of impartiality. Section 10(a)(2) just states the presumptive rule, subject to variation by mutual consent. Industry arbitration, the modern law merchant, often uses panels composed of industry insiders, the better to understand the trade's norms of doing business and the consequences of proposed lines of decision. See Lisa Bernstein, *Private Commercial Law in the Cotton Industry: Creating Cooperation Through Rules, Norms, and Institutions*, 99 Mich. L. Rev. 1724, 1728 (2001). The more experience the panel has, and the smaller the number of repeat players, the more likely it is that the panel will contain some actual or potential friends, counselors, or business rivals of the parties. Yet all participants may think the expertise-impartiality tradeoff worthwhile; the Arbitration Act does not fasten on every industry the model of the disinterested generalist judge. See *Merit Insurance Co. v. Leatherby*

Insurance Co., 714 F.2d 673, 679 (7th Cir. 1983); *Nagel v. ADM Investor Services, Inc.*, 65 F. Supp. 2d 740, 744-45 (N.D. Ill. 1999), affirmed, 217 F.3d 436 (7th Cir. 2000). To the extent that an agreement entitles parties to select interested (even beholden) arbitrators, §10(a)(2) has no role to play.

There remains the question whether this was such an agreement, to which the answer is yes and no. Party-appointed arbitrators are entitled under the ARIAS•U.S. rules to engage in *ex parte* discussions with their principals until the case is taken under advisement, but they are supposed thereafter to be impartial adjudicators. The parties assume that as a result Sphere Drake could not have appointed one of its current employees as its arbitrator. (Whether that assumption is correct depends on ARIAS•U.S. rules and practices; we need not pursue the issue.) Still, Jacks was not, and never has been, one of Sphere Drake's employees. He is a retired lawyer, until recently a partner of Mayer, Brown & Platt (now Mayer, Brown, Rowe & Maw). The district court deemed Jacks "evidently partial" because four years before the arbitration, while still at Mayer Brown, Jacks had been engaged by the Bermuda subsidiary of Sphere Drake (a United Kingdom company) as counsel on an unrelated matter that landed in arbitration but was settled before decision. It emerged in discovery compelled by the district court that Jacks had billed about 380 hours for that matter. The judge deemed Sphere Drake (U.K.) his real client because its financial interests were at stake, even though the Bermuda subsidiary signed the engagement letter and paid the fees, and even though Jacks himself thought that most of his billable time related to corporate counseling rather than to the arbitration.

Let us suppose that the district judge's inferences are sound—that Jacks spent two months of equivalent full-time service as counsel for Sphere Drake in an international insurance arbitration, four years before the unrelated arbitration with All American. Even if Jacks had been the umpire, this would not have implied "evident partiality." Indeed, Jacks could have served as a federal judge in this case without challenge on grounds of partiality, and the scope of disqualification under §10(a)(2) is considerably more confined than the rule applicable to judges. See *Health Services Management Corp. v. Hughes*, 975 F.2d 1253 (7th Cir. 1992); *Delta Mine Holding Co. v. AFC Coal Properties, Inc.*, 280 F.3d 815 (8th Cir. 2001); *International Produce Co. v. A/S Rosshavet*, 638 F.2d 548 (2d Cir. 1981). "Evident partiality" under §10(a)(2) is a subset of the conditions that disqualify a federal judge under 28 U.S.C. §455(b). A judge can't hold even a single share of a party's stock, but this would not imply "evident partiality" for purposes of §10(a)(2). The parties themselves evinced this understanding. Before the arbitration began, umpire Huggins revealed that he was an investor in American International Group, which recently had made a bid to acquire All American—yet neither side thought that this imperiled Huggins' ability to serve as the neutral.

A federal judge would be disqualified on account of prior legal work "[w]here in private practice he served as lawyer in the matter in controversy, or a lawyer with whom he previously practiced law served during such association as a lawyer concerning the matter, or the judge or such lawyer has been a material witness concerning it". 28 U.S.C.

§455(b)(2). Jacks fits none of these categories. The work he did for Sphere Drake was unrelated to the controversy with All American; no partner of Mayer Brown served "during such association" (that is, while Jacks also was a partner) as a lawyer in this dispute between Sphere Drake and All American (indeed, Sphere Drake has been represented throughout by a firm other than Mayer Brown); and neither Jacks nor any lawyer at Mayer Brown is a "material witness" in this case. Arbitration differs from adjudication, among many other ways, because the "appearance of partiality" ground of disqualification for judges does not apply to arbitrators; only *evident* partiality, not appearances or risks, spoils an award. Still, a judge's former representation of a litigant does not imply any need to disqualify under §455(a) because "his impartiality might reasonably be questioned." See *National Auto Brokers Corp. v. General Motors Corp.*, 572 F.2d 953 (2d Cir. 1978); cf. *Chitimacha Tribe v. Harry L. Laws Co.*, 690 F.2d 1157 (5th Cir. 1982). Nothing in the Code of Conduct for federal judges makes prior representation of a litigant a disqualifying event. The norm among new appointees to the bench is that once two years pass, perhaps even earlier, a judge is free to sit in controversies involving former clients. See Committee on Codes of Conduct, *Judicial Ethics Compendium* §3.6-5.

If Jacks could have served as a federal judge in this case, it is impossible to see how his background could demonstrate "evident partiality" within the meaning of §10(a)(2). See, e.g., *Gianelli Money Purchase Plan & Trust v. ADM Investor Services, Inc.*, 146 F.3d 1309 (11th Cir. 1998) (past business dealings between arbitrator and party do not

demonstrate evident partiality). "Evident partiality" for a party-appointed arbitrator must be limited to conduct in transgression of contractual limitations. No claim is made, however, that Jacks' past violated the contractual restrictions for ARIAS•U.S. arbitration. Nonetheless, All American insists that all of this is irrelevant. The problem as All American sees it is not that Jacks was partial, but that he did not disclose before the arbitration the extent of his involvement in the unrelated proceedings four years earlier. All American attributes this rule to *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145 (1968).

At the arbitrators' initial meeting, where Huggins disclosed that he had a potential financial interest in All American, Jacks said only that he had "known of Sphere Drake over the years". Before the arbitration got under way, Jacks sent a letter stating that he had neglected a more concrete connection. He wrote:

> Several years ago I provided limited corporate advice to Jonathan Crawley, then President of Sphere Drake's Bermuda subsidiary. In that capacity I recommended that my former law firm, Mayer, Brown, & Platt, be retained to represent Sphere Drake (Bermuda) Ltd. in an arbitration . . . involving a set of wholly unrelated issues which were settled shortly after the initial meeting of the Panel and Counsel.

The district judge faulted this on several counts. First, the word "former" could be read to mean that Mayer Brown was Jacks' "former" firm at the time he made

the recommendation, rather than (as was correct) at the time he wrote the letter. Second, Jacks did not reveal that when the firm took him up on the recommendation, he personally rendered legal services in the arbitration. Third, the letter did not reveal that Sphere Drake (U.K.), the parent corporation, was the real party in interest in the arbitration. Finally, the letter did not reveal the number of hours Jacks devoted to the case and left the impression that his involvement had been negligible.

Once again, let us suppose that the letter was deficient in all of these respects. How do these shortcomings demonstrate "evident partiality" when, as we have observed already, the full truth would not have disclosed even a risk of partiality? The district court treated candid and complete disclosure as a requirement in addition to disinterest. Yet that position has no purchase in the language of §10(a)(2)—or for that matter in judicial practice. A federal judge is not required to disclose his role as counsel to one litigant in an unrelated matter many years ago. Since disclosure, though often prudent, is not thought *essential* to impartial judicial service, it is hard to see how a disclosure requirement could be deemed implicit in §10(a)(2), which, to repeat, addresses only a subset of the circumstances that would disqualify a judge.

Commonwealth Coatings observes that disclosure at the outset often avoids later controversies—as Huggins's disclosure did. One can only imagine what Sphere Drake would be saying now had Huggins kept his mouth shut and then supported All American's position. Disclosure in

Commonwealth Coatings itself would have averted a problem that spoiled an award. The neutral in a tripartite arbitration was engaged in *ongoing* business relations with one of the parties, "and the relationship even went so far as to include the rendering of services on the very projects involved in this lawsuit." 393 U.S. at 146. The Court held that being on one side's payroll is a form of partiality condemned by §10(a)(2), by analogy to *Tumey v. Ohio*, 273 U.S. 510 (1927). The Justices urged arbitrators to disclose their business dealings so that similar problems would not recur.

Commonwealth Coatings did not hold, as All American would have it, that disclosure is compulsory for its own sake, and its absence fatal even if the arbitrator meets judicial standards of impartiality. See *United States Wrestling Federation v. Wrestling Division of AAU, Inc.*, 605 F.2d 313 (7th Cir. 1979) (holding an award valid even though the neutral failed to disclose that his law firm had represented one of the parties on a regular basis); *Merit*, *supra* (failure to disclose business relation many years before the arbitration does not compel vacatur of award). Nor did *Commonwealth Coatings* so much as hint that party-appointed arbitrators are governed by the norms under which neutrals operate. The point of *Commonwealth Coatings* is that the sort of financial entanglements that would disqualify a judge will cause problems for a neutral under §10(a)(2) unless disclosure is made and the parties' consent obtained.

Disclosure by a neutral may serve purposes other than flagging potential conflicts. One gets to *be* a neutral only by agreement of the party-appointed arbitrators. A potential neutral may have contractual obligations to reveal informa-

tion to those who select him. Failure to comply with a contractual requirement designed to facilitate the search for an acceptable neutral might imply that the neutral exceeded his authority, spoiling the award under 9 U.S.C. §10(a)(4). But Mangino had no power to remove Jacks, and we have not been given any reason to think that umpire Huggins wanted more information from Jacks in order to know what to make of Jacks' arguments during the panel's deliberations. For someone in Jacks' position —a party-appointed arbitrator, and one who could have presided in court under the standards of §455—failure to make a full disclosure may sully his reputation for candor but does not demonstrate "evident partiality" and thus does not spoil the award.

REVERSED

A true Copy:
Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

APPENDIX B — MEMORANDUM OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION DATED MAY 17, 2002 AND DOCKETED MAY 20, 2002

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

No. 01 C 5226

SPHERE DRAKE INSURANCE LIMITED

Plaintiff,

v.

ALL AMERICAN LIFE INSURANCE CO.

Defendant.

Judge Rebecca R. Pallmeyer

MEMORANDUM OPINION AND ORDER

Plaintiff Sphere Drake Insurance Limited ("Sphere Drake") moves to confirm an arbitration award that invalidated six reinsurance contracts between Sphere Drake and Defendant All American Life Insurance Company ("All American"). All American filed a cross motion to vacate the arbitration decision, arguing that the circumstances reveal: (1) evident partiality on the part of one of the two arbitrators who rendered the award; (2) that the hearing

denied All American fundamental fairness; (3) that the panel members exceeded their authority; and (4) that the panel exhibited a manifest disregard of the law. The arbitration award rests on a sentence that appears in All American's position statement submitted to the panel before the arbitration started. Specifically, in its position statement, All American stated that the intermediary to the reinsurance contracts was not All American's agent, a matter that had not previously been at issue in the case. Sphere Drake characterized this statement as a judicial admission, and the panel adopted that characterization. Based on this purported admission, the panel ruled that if the intermediary was not All American's agent, then All American could not have entered into any enforceable contracts, regardless of any other issues in the dispute, and, therefore, All American had no contracts with Sphere Drake to enforce. The third arbitrator filed a vigorous dissent.

For the reasons set forth below, the court concludes that because one of the two arbitrators failed to disclose a substantial attorney/client relationship with Sphere Drake, the arbitration decision must be vacated on the grounds of evident partiality.

BACKGROUND

Because the inquiry into an arbitrator's evident partiality depends on the particular facts and circumstances of each case, the events relevant to the cross motions at hand are set forth in detail below. *Morelite Const. Corp. v. New York City Dist. Council Carpenters Benefit Funds*, 748 F.2d 79, 81 (2d Cir. 1984).

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Sphere Drake is an English corporation with its principal place of business in Brighton, England. (Petition for Confirmation of Arbitration Panel's Award ("Confirmation Petition") ¶ 3, Exhibit E to Sphere Drake's Exhibits in Support of its Motion for Entry of a Protective Order ("S.D. Protective Order")). All American is an Illinois corporation with its principal place of business in Chicago, Illinois. (All American's Answer, Affirmative Defenses, and Counterclaims ("Answer") ¶ 4, Exhibit F to S.D. Protective Order.) On June 11, 1999, All American sent Sphere Drake a letter demanding arbitration with respect to balances allegedly due on several reinsurance contracts with Sphere Drake. (Confirmation Petition ¶ 7; Answer ¶ 7.) In the letter, All American designated Robert Mangino as one of the three arbitrators and requested that Sphere Drake also name an arbitrator. (All American's June 11, 1999 Arbitration Demand Letter ("Demand Letter"), Exhibit 4 to S.D. Protective Order.) Although Sphere Drake challenged whether the contracts committed the parties to arbitration, it nevertheless responded promptly, appointing Ronald A. Jacks an arbitrator for the dispute in the event the matter reached arbitration. (Sphere Drake's June 12, 1999 Letter in Response to Demand Letter, Exhibit 5 to S.D. Protective Order.) The parties agreed to have the third member of the panel, referred to as the "umpire," selected jointly by Mangino and Jacks. (Confirmation Petition ¶ 10, Answer ¶ 10.) After exchanging names, both parties agreed that Robert M. Huggins would serve as umpire and he accepted the position. (Affidavit of James Rubin ("Rubin Aff.") ¶ 13.)

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All three arbitrators have considerable experience in reinsurance arbitration, are AIDA Reinsurance and Insurance Society ("ARIAS-U.S.")[1] certified,[2] and appear on the "Umpire List" comprised of ARIAS-U.S. certified arbitrators who have served on a panel for at least three insurance or reinsurance arbitration proceedings that resulted in a final award. (Sphere Drake's Statement of Undisputed Facts for its Motion for Summary Judgment Confirming the Arbitration Award ("S.D. Statement") ¶¶ 11-14.) Huggins has participated in more than thirty-five arbitrations as an arbitrator and in at least twenty as an umpire, Jacks in more than fifty-five arbitrations as an arbitrator and in more than twenty-five as an umpire, and Mangino in more than thirty-five arbitrations as an arbitrator and four as an umpire. (*Id.* at ¶ 11.) In addition to this extensive arbitration experience, Jacks and Mangino are founding directors of ARIAS-U.S. (*Id.* at ¶ 13.) Jacks is also a past president of the U.S. chapter of AIDA, the Association International

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1. ARIAS-U.S. is an organization formed to promote the improvement of the insurance/reinsurance arbitration process and to provide the training necessary to serve effectively on an insurance/reinsurance panel. (S.D. Statement ¶ 13.)

2. To become an ARIAS-U.S. Certified Arbitrator, an individual must have at least ten years of specialized experience in the insurance/reinsurance industry, have some specified arbitration experience, be in good standing with the ARIAS-U.S., be sponsored in writing by an already certified or qualified individual, arrange for two seconding letters from certified or qualified individuals, and finally be approved as a certified arbitrator by a vote of no less than 2/3 of the full membership of the ARIAS-U.S. Board of Directors. (S.D. Statement ¶ 13.)

de Droits des Assurances, an international insurance law organization, and is currently an honorary member of its Presidential Counsel. (*Id.* at ¶ 12.)

On February 1, 2001, the parties proposed to the Panel that each side submit a position statement before the organizational meeting scheduled for April 11, 2001.[3] (*Id.* at ¶ 15.) On March 21, 2001, Sphere Drake submitted its Pre-Organizational Meeting Statement of Issues and Counterclaim ("Sphere Drake Position Statement"). (*Id.* at ¶ 16.) In its statement, Sphere Drake argued that it was not bound by the six purported contracts at issue because they were not entered into properly. (*Id.* at ¶ 17.) It further contended that those contracts were void because the intermediary, Stirling Cooke Brown Reinsurance Brokers Limited, and its affiliate, Stirling Cooke Brown Insurance Brokers Limited (collectively "Stirling Cooke"), knew that Sphere Drake's agent, Euro International Underwriters Ltd. ("EIU"), was acting in breach of its fiduciary duties in accepting the reinsurance business being brokered by Stirling Cooke. (*Id.*) Stirling Cooke, Sphere Drake alleged, knew that EIU was acting outside of its authority and had no capacity to contract.[4] (*Id.*) In this initial position paper, Sphere Drake

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3. From the time of All American's initial demand for arbitration in June 1999, to February 2001, when the parties started discussing the organizational meeting, the parties were involved in litigation in the Northern District of Illinois and the Seventh Circuit regarding whether the contracts at issue committed them to arbitration.

4. The record does not identify which of Stirling Cooke's employees are involved in the formation of the disputed contracts.

did not contest the authority of Stirling Cooke to form binding contracts on behalf of All American. Rather, the argument, as understood by both parties, concerned whether Stirling Cooke was aware that EIU did not have authority to bind Sphere Drake in the manner it did. (All American's Memorandum of Law in Support of its Motion to Vacate ("A.A.'s Motion to Vacate") at p. 6.) Notably, each of the contracting parties acted through agents: All American acted through its underwriting agent WEB Management LLP ("WEB") and Sphere Drake through its agent EIU. Stirling Cooke acted as an intermediary between the two agents, WEB and EIU. Throughout the arbitration, Sphere Drake contended that EIU acted outside of its authority when purporting to enter into the contracts on its behalf and that they are, therefore, invalid. Sphere Drake never challenged the authority of Stirling Cooke or WEB to form contracts on behalf of All American.

All American responded with its statement of the case on April 4, 2001 (All American's Position Statement"). (S.D.Statement, ¶ 18.) All American contended that Sphere Drake's argument provided no defense to enforcement of the reinsurance agreements. Specifically, All American observed that where an agent (meaning Sphere Drake's agent EIU) acts with express written authority to bind its principal (Sphere Drake), the principal may not later shift the consequences of the agent's action to a third party solely because the transaction was not as profitable as the principal had hoped. (*Id.*) (All American's Position Statement, p. 2, Exhibit A to S.D. Protective Order.) All American's submission also includes the following statement, which Sphere Drake seizes upon here: "There was no agency relationship

between Stirling Cooke and All American or between Stirling Cooke and WEB; Stirling Cooke had no authority to bind either All American or WEB and neither All American nor WEB entered into any form of agency agreement with Stirling Cooke." (*Id.* at p. 4.) This was the first time either party had addressed or even mentioned the agency relationships with respect to All American.

The parties and the arbitrators held an organizational meeting on April 11, 2001. (S.D. Statement, ¶ 20.) During this meeting, both arbitrators and the umpire disclosed their current and prior relationships with each other, with the parties and with the parties' counsel. (*Id.* at ¶ 21.) Arbitrator Jacks disclosed that, although he knew All American existed, this was his first contact with the company. (Transcript of April 11, 2001 Meeting, at p. 3, Exhibit B to S.D. Protective Order.) Regarding Sphere Drake, Jacks disclosed that he had "known of Sphere Drake over the years and of Sphere Drake's parent Odyssey," and that he was the party arbitrator for Sphere Drake on two pending arbitrations. (*Id.* at 3-4.) Umpire Huggins disclosed that he was a shareholder in American International Group, Inc., a company that had recently made a bid to acquire All American. (*Id.* at 5.) Huggins also disclosed that in early 1996, Sphere Drake's parent corporation, Fairfax, had retained him to head a due diligence team and that he also had been involved as an arbitrator for an affiliate of Sphere Drake, TIG. (*Id.*) Neither party objected to these disclosures, and the parties certified the panel as duly constituted and competent to hear and decide the dispute. (*Id.* at 6.)

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During the organizational meeting, at Sphere Drake's request and over All American's objections, the panel granted permission for Sphere Drake to submit a case-dispositive motion based on All American's statements in its position paper. (S.D. Statement, ¶¶ 22-23.) Sphere Drake argued that All American's statement in its position statement regarding the lack of agency between itself and both WEB and Stirling Cooke was a judicial admission warranting dismissal of the case on the merits with prejudice. (Sphere Drake's Motion for Judgment in its Favor on the Pleadings, at pp. 1-4, Exhibit 2 to S.D. Protective Order.) Sphere Drake contended that All American "admitted" that the reinsurance intermediary, Stirling Cooke, lacked the capacity to enter into the contracts at issue and thus no contracts were ever formed. (*Id.*)

On May 7, 2001, upon reviewing the transcript of the April meeting, Jacks announced that he realized he had neglected to disclose a prior relationship with a company related to Sphere Drake. (S.D. Statement, ¶¶ 24-25.) In his May 7 letter to the parties, Jacks explained:

> Several years ago I provided limited corporate advice to Jonathan Crawley, then President of Sphere Drake's Bermuda subsidiary. In that capacity I recommended that my former law firm, Mayer, Brown, & Platt, be retained to represent Sphere Drake (Bermuda) Ltd in an arbitration . . . involving a set of wholly unrelated issues which were settled shortly after the initial meeting of the Panel and Counsel.

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(Jacks's May 7, 2001 Disclosure Letter, Exhibit C to S.D. Protective Order.) All American did not object to Jacks's revised disclosure.

On July 5, 2001, both arbitrator Jacks and umpire Huggins, with arbitrator Mangino in strong dissent, issued the Final Award granting Sphere Drake's Motion for Judgment on the Pleadings and dismissing the arbitration on the merits with prejudice. (Final Award, Exhibit 3 to S.D. Protective Order.) In the Final Award, Jacks and Huggins stated:

> All American's [position statement] . . . is a "Pleading," as defined by the relevant authorities . . . [and] as such, All American's statement . . . is a "Judicial Admission" as that term is defined by the relevant authorities, and thus is binding on All American as a matter of law and public policy. Therefore, since All American has formally and unequivocally admitted in its pleadings that: (1) there "was no agency relationship between Stirling Cooke and All American and WEB"; (2) "Stirling Cooke had no authority to bind either All American or WEB"; and (3) "neither All American nor WEB entered into *any* form of agency agreement with Stirling Cooke" (emphasis added), Stirling Cooke . . . was not legally competent to contract with Sphere Drake or . . . EIU, and there is no need for an evidentiary hearing on this issue.

(*Id.*)

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Arbitrator Mangino voiced a strong dissent to the Final Award. He stated:

> [T]he basis of the panel majority decision [was] to give ambiguous wording on agency relationships provided in a statement of position, but clarified through briefs and oral arguments at the hearing on the Motion to Dismiss, the same weight as a pleading in a court proceeding. This technical reliance on the wording of a statement of position constitutes a denial of All American's right of due process and an extraordinary and unprecedented departure from applying industry practice and procedures to reinsurance disputes. All American was prevented from engaging in discovery, fully briefing the panel and presenting evidence and arguments at a final hearing on the merits of the dispute.

(Mangino's Dissent to Final Award, Exhibit 3 to S.D. Protective Order.) Mangino further urged that, "[i]n a motion to dismiss, especially in an arbitration proceeding, all inferences and factual issues should be construed in favor of the respondent. Here the panel did not give All American's explanation of its position on agency relationships appropriate weight." (*Id.*)

Shortly after the panel majority rendered its final decision, David Gilmartin, former in-house counsel for Continental Casualty Company ("CNA"), told Andrew Amer, counsel for All American, that Jacks had appeared as counsel of record for Sphere Drake itself in an arbitration commenced in 1996

(the "POMG Arbitration").[5] (Affidavit of Andrew S. Amer ("Amer Aff.") ¶ 2.) All American requested a transcript of the organizational meeting in the POMG Arbitration, but Sphere Drake refused, insisting that Jacks's May 7 letter adequately disclosed his involvement in the POMG Arbitration. (July 25, 2001 Letter from H.C. Wheeler to Amer, Exhibit 2 to Amer Aff.) In light of this refusal, All American served narrow discovery notices on Sphere Drake and the Mayer Brown law firm seeking production of the POMG Arbitration transcript and other information and documents regarding Jacks's attorney/client relationship with Sphere Drake. (Amer Aff. ¶ 6.) Although Mayer Brown did not raise any objections to the subpoena, Sphere Drake sought a protective order to prohibit this discovery. (Amer Aff. ¶ 7.) On October 31, 2001, this court denied Sphere Drake's motion for a protective order and granted All American's request for discovery. (Docket # 27.)

On November 14, 2001, Sphere Drake and Mayer Brown responded to All American's discovery notices. From these disclosures, All American learned that CNA commenced the POMG Arbitration in April of 1996, against Sphere Drake itself (not Sphere Drake's Bermuda subsidiary) to resolve a dispute over reinsurance coverage provided by Sphere Drake to POMG. (A.A.'s Motion to Vacate, p. 2.) The reinsurance slip at issue in the POMG Arbitration was issued on behalf of Sphere Drake and the caption of the arbitration shows that Sphere Drake was the respondent. (*Id.*)

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5. It is not clear what prompted this discussion between Gilmartin and Amer.

The discovery also revealed that it was Jacks himself, then a partner at Mayer Brown, who was actively involved as Sphere Drake's counsel in that arbitration proceeding: he billed 379.35 hours over four years and generated $132,737.50 in legal fees. (*Id.*) As a firm, Mayer Brown billed total fees of $278,771.25 on the POMG matter. (*Id.*) Mayer Brown's new client memoranda for the POMG matter listed Jacks as the billing and responsible attorney, and listed the client as "Sphere Drake Underwriting Management (Bermuda) Limited." (S.D.Statement, ¶ 35.) All American also learned that Jacks worked on other matters related to Sphere Drake: Jacks billed 13 hours in connection with arbitration against Sphere Drake concerning a reinsurance claim by North American Manufacturing Insurance Company (the "NAMIC Arbitration"). (All American's Memorandum of Law in Opposition to Sphere Drake's Motion for Summary Judgment Confirming the Arbitration Award, p. 8.) And Jacks billed another 51.50 hours providing general corporate advice in connection with two matters for Sphere Drake's Bermuda subsidiary. (*Id.*) His total fees for these other matters amounted to $22,575.00.[6] (*Id.*) All American now argues that these circumstances reveal evident partiality on Jacks's part, requiring that the arbitration award be vacated.

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6. It is unclear from the record when Jacks performed work on these other matters for Sphere Drake.

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DISCUSSION

Once a dispute has been resolved through arbitration, the role of a reviewing court is extremely limited. *Moseley, Hallgarten, Estabrook & Weeden, Inc. v. Ellis*, 849 F.2d 264, 267 (7th Cir. 1988). All American, as the party challenging the arbitration award, bears the substantial burden of proving grounds for vacation. *Middlesex Mutual Ins. Co. v. Levine*, 675 F.2d 1197, 1201 (11th Cir. 1982).

A federal court may vacate an arbitration award where the challenging party shows that there was evident partiality on the part of any of the arbitrators. 9 U.S.C. § 10(a)(2).[7] Demonstrating evident partiality is a substantial task The Seventh Circuit has explained that the showing requires "more than a mere appearance of bias." *Health Services Mgmt. Corp. v. Hughes*, 975 F.2d 1253, 1264 (7th Cir. 1992). Indeed, "[t]o set aside an award for arbitrator partiality, '[t]he interest or bias must be direct, definite and capable of demonstration rather than remote, uncertain or speculative.'" *Id.* quoting *Tamari v. Bache Halsey Stuart Inc.*, 619 F.2d

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7. The parties dispute whether or not the defenses in § 10 of the Federal Arbitration Act are available where the applicable arbitration law is an international convention, The United Nations Convention on the Recognition and Enforcement of Foreign Arbitrational Awards. 9 U.S.C. § 201 *et seq.* According to Article V(1)(e) of the Convention, however, a court in the country under whose law the arbitration was conducted may apply domestic arbitration law in deciding whether to vacate or confirm the award. Therefore, both the Convention and § 10 of the FAA may be applied here. *Nat'l Educ. Corp. v. Martin*, No. 93 C 6247, 1995 WL 622267, at *3 (N.D. Ill. Oct. 20, 1995).

1196, 1200 (7th Cir. 1980). Case law on the subject reveals a "mood. . . . of reluctance to set aside arbitration awards for failure of the arbitrator to disclose a relationship with a party." *Merit Insurance Co. v. Leatherby Insurance Co.*, 714 F.2d 673, 682 (7th Cir. 1983). The Seventh Circuit has also observed nevertheless that, despite this definite reluctance, where "circumstances are such that a man of average probity might reasonably be suspected of partiality" and "the circumstances . . . [are] powerfully suggestive of bias," the language of the Federal Arbitration Act might require disqualification. *Id.* at 681. This is not to say, however, that a party must be able to show actual bias, for such a showing might very well be impossible. *Id.* at 682.

As the Supreme Court has explained, arbitrators are required to disclose any dealings that might give rise to the appearance of bias. *Commonwealth Coatings Corp. v. Continental Cas. Co.*, 393 U.S. 145, 149 (1968). Though seemingly straightforward, this requirement is the source, as this case demonstrates, of many claims of evident partiality. Addressing this issue, the Seventh Circuit has counseled that arbitrators should err on the side of disclosure in order to prevent attacks on their decisions. *United States Wrestling Fed. v. Wrestling Div. of the AAU, Inc.*, 605 F.2d 313, 319 (7th Cir. 1979). As the Supreme Court observed, "[w]e can perceive no way in which the effectiveness of the arbitration process will be hampered by the simple requirement that arbitrators disclose to the parties any dealings that might create an impression of possible bias." *Commonwealth Coatings Corp.*, 393 U.S. at 149.

The arbitrators here purported to fulfill this disclosure requirement when, at the April 11 organizational meeting, each discussed his respective prior relationships with the parties, parties' counsel, and each other. On the basis of the seemingly benign disclosures made at this meeting, the parties certified the panel as duly constituted and competent to hear and decide the dispute.[8] All American accepted this panel under the misimpression, based on Jacks's representations at the time, that Jacks had merely "known of Sphere Drake over the years and of Sphere Drake's parent Odyssey," and that he was, at that time, the party arbitrator for Sphere Drake on two other pending matters. (Transcript of April Meeting at 4, 6-7.) Jacks stated that this account was "the nature and extent of [his] involvement to the best of [his] recollection." (*Id.* at 5.) He divulged no more about his relationship with Sphere Drake despite All American's

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8. The court is aware that most evident partiality cases concern alleged partiality on the part of the neutral arbitrator, or concern alleged partiality of panels composed entirely of purportedly neutral arbitrators. *See e.g.*, *Commonwealth Coatings Corp.*, 393 U.S. at 146; *Delta Mine Holding Co. v. AFC Coal Properties, Inc.*, 280 F.3d 815, 817 (8th Cir. 2001). Jacks was a party-appointed, as opposed to a neutral, arbitrator. The court nevertheless concludes that the parties' respective right to approve of the panel before the arbitration began could only be meaningfully exercised to the extent it was based on a full disclosure. In this situation, the parties reasonably expected that the arbitrator appointed by the opposing side would follow the disclosure rules, so that each party could make an informed decision as to whether to approve the panel. Where the parties had the right to approve or disapprove of the panel, therefore, it makes sense to be equally concerned about the disclosures made by the party-appointed arbitrators, as about those of the neutral arbitrator.

counsel's pointed attempts to gauge its extent. For example, counsel for All American asked Jacks about the pending arbitrations: when they would get underway and whether the evidence would overlap with the present matter. (*Id.* at 6-7.) Upon receiving Jacks's assurances that he would not consider any evidence or insight gained from the other Sphere Drake arbitrations, All American's counsel was satisfied with Jacks's presence on the panel. (Id. at 7, 13.)

Jacks's apparent lack of candor at this meeting is troublesome. That Jacks did not fully explain the depth of his prior involvements with Sphere Drake is, by itself, disappointing. Worse, however, Jacks implied that he had no prior involvements with the company at all—to the contrary, he had merely "known of Sphere Drake." Sphere Drake does not now suggest that Jacks somehow forgot about his past representation of Sphere Drake. Indeed, Sphere Drake has not offered, nor can the court conceive of, any satisfying explanation for Jacks's statements.

Nor was this Jacks's only misleading disclosure. In his May 7, 2001 letter, Jacks stated that at the April meeting, he "neglected to disclose that several years ago [he] provided *limited* corporate advice to . . . *Sphere Drake's Bermuda subsidiary.*" (Jacks's May 7, 2001 Letter, emphasis added.) He further stated that it was in this capacity that he "recommended that [his] former law firm, Mayer, Brown & Platt, be retained to represent Sphere Drake (Bermuda) Ltd. in an arbitration . . . involving a set of wholly unrelated issues. . . ."[9]

9. This arbitration was later identified by All American as the POMG Arbitration.

(Jacks's May 7, 2001 Letter.) On its face, this disclosure was no cause for alarm—a plain reading disclosed only that Jacks gave Sphere Drake limited corporate advice and suggested that Sphere Drake retain a law firm with which he was no longer affiliated. The reader would likely conclude that Jacks forgot to mention this matter earlier because, after all, he provided only limited advice before Sphere Drake retained his former colleagues at Mayer Brown. Although the letter conveys this impression, it is not at all accurate: As All American learned after the final award, Jacks's "limited corporate advice" in fact amounted to more than four hundred hours of work performed over four years. And while "former law firm" was an accurate description of Mayer, Brown & Platt at the time Jacks wrote the letter, Mayer, Brown & Platt was not his former law firm at the time he advised Sphere Drake to retain it. To the contrary, Jacks was a partner of Mayer, Brown at the time. He "referred" Sphere Drake to his own current firm, and he himself performed a great deal of the legal work for the client.

Furthermore, Jacks's assertion that he represented only the Bermudan subsidiary of Sphere Drake is plainly inaccurate. The fact that Mayer, Brown & Platt's billing records identify the Bermuda subsidiary as the party charged for the firm's services is not conclusive as to the identity of Jacks's client. Jacks was counsel of record for Sphere Drake itself in the POMG arbitration. Sphere Drake was the named reinsurer on the contract in dispute in that arbitration, and it assumed 100% of the risk. The Bermuda subsidiary Jacks later characterized as his client merely acted as the underwriting agent on the disputed reinsurance slip and assumed none of its liability. Jacks billed a total of 379.35 hours to

this matter, earning a fee of $132,737.50. He also failed to disclose 13 hours of work on behalf of Sphere Drake in the NAMIC Arbitration, and another 51.25 hours of advice to Sphere Drake's Bermuda subsidiary.

All American argues that Jacks's failure to disclose the substantial work he did on behalf of Sphere Drake demonstrates his evident partiality, urging that the only explanation for his silence is a purposeful intent to deceive All American. Courts are disinclined to set aside arbitral awards based on evident partiality, in part because it is rare that a party can make a showing sufficient to warrant a such finding. Mindful of these precedents, the court finds that All American has met its substantial burden in this case.

First, it is clear that the relationship between Jacks and Sphere Drake was more substantial than the relationships the Seventh Circuit has found to be trivial or lacking such personal, professional, social or financial intimacy as would "cast serious doubt on [the arbitrator's] impartiality." *Merit Ins. Co.*, 714 F.2d at 680. For example, in *Merit*, where the neutral arbitrator did not disclose that he had worked under the president of one of the parties when they both worked for another company, the Seventh Circuit observed that the relationship had ended 14 years before the arbitration, it had been distant and impersonal, and the arbitrator had no financial stake in the arbitration's outcome. *Id.* The court concluded that the failure to disclose a relationship of this kind did not constitute evident partiality. *Id.*

Similarly, in *Health Services Mgmt. Corp.*, two of three arbitrators each disclosed that they knew the architect involved in the arbitration. One had worked in the same office

20 years before the arbitration and saw the architect about once a year since that time, and the other reported that the architect worked at the same firm with him for a summer years earlier and that he had seen him twice in the last four or five years at meetings. 975 F.2d at 1255. Both indicated that their prior relationships would have no prejudicial effect on their decision, and the opposing party's counsel stated that he would rely on these representations. *Id.* The Seventh Circuit found that counsel had accepted the arbitrators with knowledge of their past relationship to the party architect. The court noted, further, that the relationships at issue were minimal and that no close association ever existed between either of the arbitrators and the party architect. *Id.* at 1264. In another case, where the arbitrator's law firm, but not the arbitrator himself, represented an entity indirectly affilicated with one of the arbitral parties, the Seventh Circuit concluded that the connection was "too 'remote, uncertain, and speculative' to require the arbitration decision [involving the U.S. Wrestling Federation] to be set aside." *United States Wrestling Federation v. Wrestling Division of the AAU, Inc.*, 605 F.2d 313, 315-16 (7th Cir. 1979.)

In this court's view, Jacks's four-year attorney-client relationship with Sphere Drake demonstrates a far more intimate connection to Sphere Drake than any of the more tangential relationships that the Seventh Circuit found inconsequential for evident partiality purposes. What is at least as important as the connection itself, however, is the negligent or even intentional inadequacy of Jack's disclosure of the relationship. The court is unaware of any case where an arbitrator has offered such an ineffective description of his connection to a party. In one case that appears to come

close, the court vacated the resulting arbitration award: In *Kaiser Foundation Hospitals, Inc. v. Coburn*, 19 Cal.App. 4th 513 (Cal.Ct.App.1993), the neutral arbitrator never disclosed the fact that he had served previously several times as party arbitrator for Kaiser Foundation Hospitals, Inc. ("Kaiser"). Two years later, long after he was selected, Kaiser's counsel wrote a letter formally accepting the neutral arbitrator, pointing out that Kaiser accepted him "'even though he has sat as a claimant's party arbitrator in other cases against my client, as a neutral in other cases and even as a party arbitrator on behalf of my client.'" *Id.* at 516. Affirming the trial court's decision vacating the award, the court observed that the arbitrator's failure to reveal his relationship with a party might be overcome if the important facts are actually revealed. *Id.* at 517. It concluded, however, that the "terse, and essentially misleading, phraseology of counsel's letter of acceptance, did not adequately fulfill that obligation here," and upheld trial court's decision to vacate the arbitration award. *Id.* The letter written by counsel in *Kaiser* was arguably more informative and straightforward about the fact that the arbitrator at issue had been a party arbitrator for Kaiser in the past, than was Jacks's letter about his past legal representation of Sphere Drake.

Significantly, courts are quick to conclude that there was no evident partiality where an arbitrator has offered a straightforward and honest disclosure of the relationship at issue. *Tamari v. Bache Halsey Stuart Inc.*, 619 F.2d 1196, 1199 (7th Cir. 1980), illustrates the importance of such disclosure. In that case, an employee of Bache Halsey Stuart Inc. testified at an arbitration proceeding concerning the production of certain documents pursuant to subpoena.

Id. at 1198. Prior to giving this testimony, the employee had entered negotiations for employment with the employer of one of the arbitrators. *Id.* The negotiations remained confidential until an agreement was reached, but once he agreed to work for the arbitrator's employer, the testifying witness promptly disclosed the new employment relationship to the panel and the parties. *Id.* at 1199. The arbitrator at issue had nothing to do with the negotiations, nor was he involved in the decision to hire the witness; he nevertheless volunteered to withdraw and did withdraw upon the objecting party's request. *Id.* In an action to set aside the arbitration award, the objecting party argued that the taint from the withdrawn arbitrator's presence on the panel required that the entire panel recuse themselves, and that the failure to do so demonstrated evident partiality. *Id.* at 1198. The Seventh Circuit was unpersuaded; the court concluded that even if the withdrawn arbitrator "had some nontrivial interest in the proceedings because his employer had hired the employee of a party, any appearance of bias was dispelled by the forthright manner in which the situation was handled once it became known." *Id.* at 1199.

In *United States Wrestling Federation*, the Seventh Circuit emphasized the Supreme Court's guidance that disclosure should be the default: "[W]here the arbitrator has a substantial interest in a firm which has done more than trivial business with a party, that fact must be disclosed. If arbitrators err on the side of disclosure, as they should, it will not be difficult for courts to identify those undisclosed relationships which are too insubstantial to warrant vacating the award." 605 F.2d at 319, quoting *Commonwealth Coatings*, 393 U.S. at 150. An arbitrator in that case did not

disclose that attorneys in his law firm represented Northwestern University. In an appeal from the district court order confirming the arbitration award, the Wrestling Division argued that because the United States Wrestling Federation was principally funded by the National Collegiate Athletic Association ("NCAA"), and Northwestern University is a member of the NCAA, the arbitrator's failure to disclose his law firm's relationship to Northwestern demonstrated evident partiality. *United States Wrestling Federation*, 605 F.2d at 317-18. The Seventh Circuit concluded that the arbitrator's connection to the United States Wrestling Federation was too remote and trivial to render the failure to disclose it problematic. *Id.* In reaching this conclusion the court noted that it needed to assess the arbitrator's connection to the Wrestling Federation only because the arbitrator's apparent failure to disclose left the arbitration award subject to attack. *Id.* at 320.

The Eleventh Circuit has also emphasized that evident partiality is shown where an "arbitrator knows of, but fails to disclose, information which would lead a reasonable person to believe that a potential conflict exists." *Gianelli Money Purchase Plan and Trust v. ADM Investor Servs., Inc.*, 146 F.3d 1309, 1312 (11th Cir. 1998). The sole arbitrator in that case did not disclose that his law firm had represented Kent Kelley, the individual whose alleged wrongdoing led to an agency-theory claim against ADM. *Id.* Kelley was president of Basic Commodities, Inc., a company which contracted to bring commodities trading customers to ADM, *Id.* at 1310. Plaintiff Gianelli was one such customer. When his account went south, Gianelli filed a claim against ADM on the theory that ADM was responsible for Kelly's

misconduct. *Id.* Prior to the arbitration, Gianelli discovered that the arbitrator's firm represented Kelley in a securities case. *Id.* The arbitrator himself was unaware of this representation by other lawyers in his firm, while Kelley claimed (falsely) that this representation by the arbitrator's firm was an isolated occurrence. *Id.* Following an award in ADM's favor, Gianelli learned that the arbitrator's firm had in fact represented Kelley on a number of occasions and moved to vacate the award on evident partiality grounds. *Id.* The Eleventh Circuit reversed the district court's decision vacating the arbitration award because there was no evidence that the arbitrator was actually aware of his firm's representation of Kelley. *Id.* at 1313. As noted, Sphere Drake has not offered any such explanation for Jacks's failure to be completely forthcoming. Nor could Jacks, who personally represented Sphere Drake as recently as 1997, credibly assert that he was unaware of his firm's involvement on Sphere Drake's behalf.

As reflected in the cases reviewed here, courts are often persuaded that there is no evident partiality when the arbitrator did not know about the relationship alleged to constitute a conflict. *See e.g.*, *Al-Harbi v. Citibank, N.A.*, 85 F.3d 680, 682 (D.C. Cir. 1996), *Peoples Security Life Ins. Co. v. Monumental Life Ins. Co.*, 991 F.2d 141, 145-46 (4th Cir. 1993). And conversely, where the arbitrator knew of, but failed to disclose, a significant relationship to a party, courts have found evident partiality. *Olson v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 51 F.3d 157, 158-59 (8th Cir. 1995) is such a case. In *Olson*, one of the arbitrators disclosed that he was employed by a financial services firm, but did not disclose that he was its vice-president and chief financial

officer. *Id.* at 159. He further failed to disclose that his firm did a substantial amount of business with Merrill Lynch, a party to the arbitration. *Id.* The court found that as a high-ranking officer in a firm doing more than trivial business with a party to the arbitration, the arbitrator's failure to disclose the relationship showed evident partiality and required that the award be vacated. *Id.* at 160. Similarly, in *Middlesex Mutual Ins. Co.*, the neutral arbitrator knew, but did not disclose, that his family-owned insurance company was involved in litigation with Middlesex. 675 F.2d at 1201-02. The neutral arbitrator and one other arbitrator rendered a $1,200,000 award in favor of the claimant and against Middlesex. *Id.* at 1199. Finding the arbitrator's claimed bad-memory excuse "spurious," the Eleventh Circuit concluded that the failure to disclose this significant relationship displayed evident partiality and upheld the district court's decision to vacate the award.

In the case before this court, Sphere Drake does not argue that Jacks made a forthright and accurate disclosure. His first statement that he merely "knew of" Sphere Drake, paired with his second disclosure that he had given the company "limited corporate advice" and advised them to retain his "former law firm," were at minimum deficient and at worst might be construed as a calculated effort to obscure his more significant connections to Sphere Drake. The Supreme Court in *Commonwealth Coatings Corp.* faced a similar situation when it found evident partiality on the part of an arbitrator in that case: "[W]e have no reason, apart from the undisclosed business relationship, to suspect him of any improper motives," but neither the arbitrator nor the party "gave to petitioner even an intimation of the close financial relations

that had existed between them for a period of years." 393 U.S. at 147-48. In *Commonwealth*, the neutral arbitrator did not disclose that, as an engineering consultant, he had rendered services to one of the parties to the arbitration on a repeated and significant basis over a five year period, and had even provided consulting services on the very projects at issue in the arbitration. *Id.* at 146. The Supreme Court concluded that the failure to disclose this significant relationship was, standing alone, sufficient to warrant setting aside the arbitration award on the basis of the arbitrator's evident partiality. *Id.* at 149. Likewise, this court concludes that Jacks's failure to disclose, and apparent attempts to conceal, his past attorney-client relationship with Sphere Drake establishes the kind of intimate professional relationship that casts serious doubt on Jacks impartiality. His behavior deprived "the parties who are in the best position to judge an arbitrator's partiality, a chance to reject or accept an arbitrator with full knowledge of the arbitrator's connections." *Olson*, 51 F.3d at 160.

The court recognizes its role is not to review the substance of the panel's decision. Nevertheless, the court notes at least some concern about the unique manner in which the panel swiftly resolved the dispute in Sphere Drake's favor, without hearing the evidence and without considering the merits of the case at all. *Compare Tinaway v. Merrill Lynch & Co., Inc.*, 658 F. Supp. 576, 579 (S.D.N.Y. 1987) (where court could not infer from the record any basis for the arbitrators' decision to hold Merrill Lynch liable, but to reduce the damage award from the claimed $35,720 loss, to just $2,000, the court concluded this unexplained reduction could "only represent 'evident partiality' on the part of the arbitrators towards Merrill Lynch.")

Appendix B

Finally, Sphere Drake contends that All American waived its right to assert evident partiality by failing to raise the issue after Jacks's supplemental disclosure letter. Typically, courts will not allow a party to raise an evident partiality claim as a ground for vacating an award where the party was aware of, but failed to raise the claim during the arbitration process. *Kiernan v. Piper Jaffray Cos.*, 137 F.3d 588, 593 (8th Cir. 1998) (party made strategic choice to go forward with arbitrator on the panel after receiving supplemental disclosures from her that raised concerns about potential evident partiality and could not, after losing the arbitration, raise evident partiality claim because they chose to ignore the basis for that claim during the arbitration); *Cook Indus. v. Itoh & Co.*, 449 F.2d 106, 107-08 (2d Cir. 1981) (party was fully aware of arbitrator's relationship to opposing party during arbitration but raised no objection during proceedings, and could not after receiving an unfavorable result "complain of a situation of which he had knowledge from the first"). The claim is not waived here, however. As this court has noted, the supplemental disclosure was misleading, far from complete, and, contrary to Sphere Drake's contention, does not clearly disclose a prior attorney/client relationship with Sphere Drake. This was not a situation where All American knew that Jacks had a potentially substantial connection to Sphere Drake and chose to overlook it in the interest of moving forward. To the contrary, Jacks's letter conveyed the impression that his only relationship to Sphere Drake was that he had provided limited corporate advice to its subsidiary. All American was not unreasonable in accepting this disclosure, and to the extent Jacks understated or misrepresented his relationship with Sphere Drake, All American did not waive its right to raise the issue.

Appendix B

CONCLUSION

For the above reasons, Sphere Drake's motion for summary judgment confirming the arbitration award (36-1) is denied. The award in favor of Sphere Drake is vacated without prejudice to further arbitration proceedings.

ENTER:

Dated: May 17, 2002

s/ Rebecca R. Pallmeyer
REBECCA R. PALLMEYER
United States District Judge

APPENDIX C — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT DENYING PETITION FOR REHEARING DATED NOVEMBER 4, 2002

UNITED STATES COURT OF APPEALS
For the Seventh Circuit
Chicago, Illinois 60604

November 4, 2002

Before

Hon. FRANK H. EASTERBROOK, Circuit Judge

Hon. MICHAEL S. KANNE, Circuit Judge

Hon. TERRENCE T. EVANS, Circuit Judge

No. 02-2458

SPHERE DRAKE INSURANCE LIMITED,

Plaintiff-Appellant,

v.

ALL AMERICAN LIFE INSURANCE COMPANY,

Defendant-Appellee.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

Appendix C

No. 01 C 5226
Rebecca R. Pallmeyer, *Judge*.

Order

Defendant-appellee filed a petition for rehearing and rehearing en banc on October 23, 2002. No judge in regular active service has requested a vote on the petition for rehearing en banc, and all of the judges on the panel have voted to deny rehearing. The petition for rehearing is therefore DENIED.

(2)

Supreme Court, U.S.
FILED
MAR 7 2003

No. 02-1168

IN THE

Supreme Court of the United States

AMERICAN GENERAL LIFE INSURANCE COMPANY,
Petitioner,

v.

SPHERE DRAKE INSURANCE LIMITED,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF FOR RESPONDENT IN OPPOSITION

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46 pp
& f/o

QUESTION PRESENTED

Whether, pursuant to the "evident partiality" standard of § 10(a)(2) of the Federal Arbitration Act, 9 U.S.C. § 10(a)(2), an arbitration award must be vacated merely because a party-appointed arbitrator failed to make a full disclosure of his prior relationship to the parties, even though the undisclosed facts themselves would not demonstrate the arbitrator's "evident partiality."

CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6 of the Rules of this Court, respondent Sphere Drake Insurance Limited states the following:

Sphere Drake Insurance Limited is a wholly owned subsidiary of Fairfax Financial Holdings Limited, a Canadian corporation that is publicly traded on the Toronto Stock Exchange and the New York Stock Exchange. Fairfax Financial Holdings Limited has no parent company, and no publicly held company owns 10% or more of its stock.

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INTRODUCTION

This case involves a dispute between two insurance companies over alleged contracts to provide reinsurance. Pursuant to a post-contract agreement, the dispute was submitted to a panel of three arbitrators, consisting of two arbitrators appointed by the parties and a neutral umpire. A majority of the arbitrators determined that no contracts had been formed between the parties because petitioner had disavowed its putative agent, which had entered into the alleged agreements with respondent's agent. Absent an agency relationship, petitioner's putative agent had no power to bind petitioner, and thus no contract between petitioner and respondent could be established.

As the case proceeded to the courts to enforce the arbitration decision, the issue became whether the party arbitrator selected by respondent Sphere Drake failed to disclose information about his prior relationship with Sphere Drake and thereby demonstrated evident partiality. In holding that the incomplete disclosure did not demonstrate evident partiality, the court of appeals applied well-settled legal principles to the facts and concluded that the arbitration was not tainted by bias. Petitioner cannot cite a single case to support its extraordinary contention that this Court should engraft onto the plain language of § 10(a)(2) of the Federal Arbitration Act ("FAA"), 9 U.S.C. § 10(a)(2), a requirement that a court must vacate an arbitration award if a party-appointed arbitrator makes an incomplete disclosure of his prior relationship to the parties even when the undisclosed information does not rise to the statutory standard of "evident partiality." Further review therefore is unwarranted.

STATEMENT

1. In a normal set of transactions between an arms-length reinsurer and reinsured, the reinsurer will set the premium at a level at which it can still make a profit after

covering the expected losses.[1] That normal financial model for reinsurance, however, was turned on its head by the agents for All American and Sphere Drake in the situation at issue. Instead of charging its reinsureds a sufficient premium to cover its anticipated losses and still post a small profit – as would be the case in the normal reinsurance arrangement – All American charged an inadequate premium for the risks it assumed. All American then sought to pass the majority of expected losses to Sphere Drake through reinsurance from Sphere Drake that was allegedly obtained by All American's putative agent from Sphere Drake's agent. The alleged contracts between All American and Sphere Drake had the certain consequence (because of the nature of the coverage and expected losses at issue) of requiring Sphere Drake to pay out losses far in excess of the premium that it received, in effect ensuring a profit to All American while guaranteeing a loss to Sphere Drake and a depletion of Sphere Drake's capital. Sphere Drake alleged that this conspiracy to defraud it was hatched by All American's putative agent Stirling Cooke Brown Reinsurance Brokers Limited ("Stirling Cooke") and involved a Ponzi-like scheme that generated brokerage commissions to Stirling Cooke at each turn of the scheme from reinsurer to reinsurer. *See* C.A. App. 201-27.[2] The more money taken out in profit and brokerage fees, the less was available to cover losses for the reinsurers down the line. Like other Ponzi schemes, at some point that house of financial cards would collapse of its own weight.

The process of creating this fraudulent series of alleged contracts was the subject of a complicated and protracted investigation, resulting in a year-long trial for fraud in the United Kingdom that ended in December 2002 and

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[1] The frequency and severity of workers compensation losses, which was the business reinsured here, can be predicted with relative confidence based on statistical data for prior years.

[2] "C.A. App." refers to the appendix to the brief filed by Sphere Drake in the Seventh Circuit.

awaits a decision. Sphere Drake brought the U.K. action against All American's agent in placing the reinsurance at issue, Stirling Cooke, and Sphere Drake's agent for accepting the reinsurance, European International Underwriters Ltd. ("EIU"). Stirling Cooke, acting for All American and other ceding companies, had placed a total of 112 contracts with EIU during the 18-month period that EIU was in operation. Like most of the other contracts that Stirling Cooke brokered to EIU, an important feature of the contracts at issue here is that they were consummated not by officers or employees of All American and Sphere Drake, but rather by companies purporting to act as the agents for All American and Sphere Drake.

Following an investigation of EIU's activities, Sphere Drake informed All American that Sphere Drake was not bound by those purported reinsurance contracts because Stirling Cooke had fraudulently colluded with EIU and induced EIU to breach the fiduciary duties EIU owed to Sphere Drake. On June 11, 1999, All American rejected Sphere Drake's assertion of fraud and made a demand for arbitration based on the seven purported reinsurance contracts between the parties, in the process also designating its party-appointed arbitrator, Robert Mangino. On July 12, 1999, Sphere Drake responded with respect to six of the supposed contracts, conditionally appointing Ronald A. Jacks as its party-appointed arbitrator and also questioning whether the "slips" that evidenced the alleged contracts committed the parties to arbitrate their disputes.[3] The parties subsequently agreed to submit the dispute raised with respect to six of the seven contracts to an arbitration panel consisting of the two party-appointed arbitrators who had already been named and a third arbitrator nominated by both parties to serve as umpire.[4]

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[3] A slip is an abbreviated version of a full reinsurance contract and contains the essential terms of the agreement. An example of the slips at issue is reproduced at App., *infra*, 1a-5a.

[4] The seventh alleged contract is the subject of litigation in the United States District Court for the Northern District of Illinois,

The parties then jointly appointed Robert Huggins as umpire.

Prior to the organizational meeting of the arbitration, which was set for April 11, 2001, the parties submitted position statements detailing their respective claims and defenses. By agreement, Sphere Drake submitted its statement first, in which it argued that the six purported contracts were void *ab initio* because All American's putative agent, Stirling Cooke, knew that Sphere Drake's agent, EIU, lacked the authority to accept (on behalf of Sphere Drake) the business that Stirling Cooke brokered. Sphere Drake also argued that Stirling Cooke had colluded with EIU to defraud Sphere Drake. In its response, All American denied that Stirling Cooke was All American's agent: "There was no agency relationship between Stirling Cooke and All American or between Stirling Cooke and WEB[5]; Stirling Cooke had no authority to bind either All American or WEB and neither All American nor WEB entered into any form of agency agreement with Stirling Cooke." Pet. App. 17a-18a (internal quotation marks omitted).

At the organizational meeting, both the arbitrators and the umpire disclosed their prior relationships with each other, the parties, and the parties' counsel. Arbitrator Jacks stated that he was aware of All American's existence, but that this was his first contact with the company. *See id.* at 18a. Jacks further reported that he had "known of Sphere Drake over the years and of Sphere

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Sphere Drake Ins. Ltd. v. All American Life Ins. Co., Case No. 99 C 4573 (Judge William T. Hart), and is not part of the litigation before this Court. That case is on remand from the Seventh Circuit's decision reported at 256 F.3d 587 (2001).

[5] WEB Management LLP was All American's managing general agent pursuant to a written contract with All American, which granted WEB authority to accept and cede reinsurance on All American's behalf. See C.A. App. 48. WEB was also affiliated with Stirling Cooke. *See id.* at 204.

Drake's parent Odyssey," and that he was the party arbitrator for Sphere Drake on two pending arbitrations. *Id.* (internal quotation marks omitted). Umpire Huggins disclosed that he was a shareholder in American International Group, Inc., which had recently made a bid to acquire All American's parent company. *Id.* Huggins further related that, in early 1996, Sphere Drake's parent corporation, Fairfax Financial Holdings Limited, had retained him to head a due diligence team and that he also had been involved as an arbitrator for one of Sphere Drake's affiliates. *Id.* Neither party objected to those disclosures, and the parties certified the panel to decide the dispute.

At the organizational meeting, the parties further agreed to allow *ex parte* contacts between the parties and their respective arbitrators through the end of discovery in the arbitration. The panel also unanimously granted Sphere Drake's request to submit a case-dispositive motion. Sphere Drake explained to the panel that All American had admitted in its response to Sphere Drake's position statement that Stirling Cooke was not its agent and had no authority to bind All American. Sphere Drake further explained that the only evidence of contracts between the parties was the offers, in the form of reinsurance "slips," extended to EIU by Stirling Cooke, purportedly acting for All American. The "slips" were then accepted by EIU, acting for Sphere Drake. If Stirling Cooke was not All American's agent, and therefore had no authority to bind it, no contract existed between All American and Sphere Drake as a matter of elementary contract law.

On May 7, 2001, after reviewing the transcript of the April organizational meeting, Arbitrator Jacks announced that he realized he had neglected to disclose a prior relationship with a company related to Sphere Drake. He explained to the parties, in writing, that he had "provided limited corporate advice to Jonathan Crawley, then President of Sphere Drake's Bermuda subsidiary. In that

capacity I recommended that my former law firm, Mayer, Brown, & Platt, be retained to represent Sphere Drake (Bermuda) Ltd. in an arbitration . . . involving a set of wholly unrelated issues which were settled shortly after the initial meeting of the Panel and Counsel." Pet. App. 19a (ellipsis in original). All American asked no questions about this information and did not object to the revised disclosure. *See id.* at 20a.

After Jacks made the revised disclosure, Sphere Drake filed its case-dispositive motion and supporting brief for a final award based on All American's admission in its position statement. Sphere Drake explained that the panel should treat All American's position statement as a pleading and its representation that Stirling Cooke had no authority to bind All American as a judicial admission. Sphere Drake contended that a party should be held to its representations to an arbitration panel in the same way that a party is held to its representations in court; without such a binding rule, parties could readily subvert the dispute resolution process. Moreover, Sphere Drake explained, in prior litigation between the parties with respect to the very same purported contracts, the United States District Court for the Northern District of Illinois had ruled that the position statements in an arbitration were the equivalent of pleadings. *See* C.A. App. 109. On the merits, Sphere Drake set forth All American's unequivocal statement that Stirling Cooke was not its agent and lacked authority to bind All American. *See id.* at 107-09. Because the only evidence of the existence of the supposed contracts was the slips that had been presented by Stirling Cooke to EIU for acceptance, All American's admission of Stirling Cooke's lack of authority was dispositive of the case. *See id.* at 112-14. Without authority from All American, Stirling Cooke could not make a valid offer to EIU when it presented the slips representing the offer to contract and thus could not form a valid contract.

On July 5, 2001, Umpire Huggins and Arbitrator Jacks issued a final award (over the dissent of Arbitrator Man-

gino) granting Sphere Drake's motion for judgment on the pleadings and dismissing the arbitration on the merits with prejudice. *See* Pet. App. 20a. The panel majority held that All American's position statement was dispositive of the case:

> All American's [position statement] . . . is a "Pleading," as defined by the relevant authorities . . . [and] as such, All American's statement . . . is a "Judicial Admission" as that term is defined by the relevant authorities, and thus is binding on All American as a matter of law and public policy. Therefore, since All American has formally and unequivocally admitted in its pleadings that: (1) there "was no agency relationship between Stirling Cooke and All American and WEB"; (2) "Stirling Cooke had no authority to bind either All American or WEB"; and (3) "neither All American nor WEB entered into *any* form of agency agreement with Stirling Cooke" (emphasis added), Stirling Cooke . . . was not legally competent to contract with Sphere Drake or . . . EIU, and there is no need for an evidentiary hearing on this issue.

Id. (brackets and ellipses in original). Arbitrator Mangino dissented, expressing the view that the wording in All American's position statement was ambiguous as to the agency relationship and that the panel should have conducted fact finding. *Id.* at 21a.

2. Sphere Drake moved in the district court to confirm the arbitration award, while All American filed a cross-motion to vacate the award on the grounds that Jacks was partial, the hearing was unfair, the arbitrators exceeded their authority, and the award was issued in manifest disregard of the law. *See* Pet. App. 12a-13a. All American sought and obtained discovery on Arbitrator Jacks' involvement with Sphere Drake during the period in which he had been a partner at Mayer, Brown & Platt. The district court granted All American's cross-motion to vacate the award. The court concluded that All American's post-arbitration discovery had revealed that: Sphere Drake

itself (rather than its Bermuda subsidiary) had been a party to the arbitration in which Mayer, Brown acted as counsel; Jacks himself had billed 379.35 hours over four years on that matter (thereby generating $132,737.50 in legal fees); and Mayer, Brown had billed total fees of $278,771.25 on the matter. *Id.* at 22a-23a. Jacks was also listed on the law firm's records as the billing and responsible attorney and had provided other legal service to Sphere Drake's Bermuda subsidiary in several matters, one totaling 13 hours of work and two others totaling 51.5 hours of work. *Id.* at 23a. Based on that evidence, the district court concluded that Jacks' failure to disclose this information demonstrated the requisite partiality to warrant overturning the arbitration award because the disclosure was inadequate and not completely forthcoming.

3. Sphere Drake appealed the decision, arguing that the district court had applied an incorrect standard to determine evident partiality and ignored important facts. First, the district court had not taken into account that Jacks had retired from Mayer, Brown on December 31, 1997, four years before his disclosure in the arbitration. Second, the district court had not considered that it was Sphere Drake's Bermuda subsidiary, and not Sphere Drake, that had retained, directed, and paid Mayer, Brown. The district court had also ignored the evidence that Sphere Drake's Bermuda subsidiary had underwritten the contract (and issued the contract in the name of Sphere Drake) in the dispute disclosed by Jacks and had directed the defense of the dispute; further, the Bermuda subsidiary was the only client listed on Mayer, Brown's records, and both Sphere Drake and its Bermuda subsidiary had been sold and their management changed at about the same time that Jacks had retired from Mayer, Brown – four years prior to the incomplete disclosure.

The Seventh Circuit reversed. Pet. App. 1a-11a. In an opinion by Judge Easterbrook, the court of appeals explained that Jacks had served more than 25 times as an "umpire" in arbitrations, having been selected "by party-

named arbitrators who relied on his reputation for legal acumen and impartiality." *Id.* at 2a-3a. The court also noted that "Huggins decided that Sphere Drake was entitled to victory on the ground that All American had disavowed Stirling Cooke Brown Reinsurance Brokers as its agent (a tactic apparently designed to avoid any risk that Stirling Cooke, which placed the reinsurance through EIU, would be found to know about EIU's limited authority)." *Id.* at 3a. The court then observed that All American challenged the arbitration because "it did not like the result" of the very arbitration process that it had "demanded." *Id.*

The court noted the unprecedented nature of the district court's ruling to overturn the arbitration award – "the first time since the Federal Arbitration Act was enacted in 1925 that a federal court has set aside an award because a party-appointed arbitrator on a tripartite panel, as opposed to a neutral, displayed 'evident partiality.'" *Id.* The court explained that party-appointed arbitrators are "*supposed* to be advocates" for the parties who appoint them, "[y]et no one believes that the predictable loyalty of these designees spoils the award." *Id.*

The court then analyzed the particular facts of Jacks' involvement with Sphere Drake. The court explained that "Jacks could have served as a federal judge in this case without challenge on grounds of partiality, and the scope of disqualification under § 10(a)(2) is considerably more confined than the rule applicable to judges." *Id.* at 6a (citing cases). The court then noted that "evident partiality," the standard under § 10(a)(2), is a "subset of the conditions that disqualify a federal judge under 28 U.S.C. § 455(b)." *Id.* The court observed that a federal judge may not own a single share of a party's stock – to do so would create "evident partiality" – but the parties themselves had agreed that such a standard would not be applied to the arbitration panel because Umpire Huggins himself had "revealed that he was an investor in American International Group, which recently had made a bid

to acquire All American – yet neither side thought that this imperiled Huggins' ability to serve as the neutral." *Id.*

As for Jacks' prior representation of Sphere Drake, the court described the disqualification standard for a federal judge sitting on a case in which he had represented a party. *Id.* at 6a-7a. Invoking the judicial codes of conduct, the court concluded that prior representation of a litigant in this circumstance was not "a disqualifying event." *Id.* at 7a. Based on the facts presented, the court reasoned that, "[i]f Jacks could have served as a federal judge in this case, it is impossible to see how his background could demonstrate 'evident partiality' within the meaning of § 10(a)(2)." *Id.* (citing cases).

The court specifically took issue with All American's characterization of *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145 (1968), noting that it "did not hold, as All American would have it, that disclosure is compulsory for its own sake, and its absence fatal even if the arbitrator meets judicial standards of impartiality." Pet. App. 10a. The court stressed that *Commonwealth Coatings* simply did not address the issue presented here: whether "party-appointed arbitrators are governed by the norms under which neutrals operate." *Id.* Rather, "[t]he point of *Commonwealth Coatings* is that the sort of financial entanglements that would disqualify a judge will cause problems for a neutral under § 10(a)(2) unless disclosure is made and the parties' consent obtained." *Id.* Accordingly, the court reversed the district court's judgment vacating the arbitration award.

The court of appeals denied All American's petition for rehearing en banc without dissent. *Id.* at 39a-40a. The case has now returned to the district court for proceedings on All American's other three challenges to the arbitration award. Under a stipulated schedule, All American has already filed its renewed motion to vacate the award, and briefing is scheduled to be completed by March 28, 2003. *See* App., *infra*, 6a.

REASONS FOR DENYING THE PETITION

I. The decision below is consistent with the plain language of FAA § 10(a)(2)'s "evident partiality" standard and this Court's decision in *Commonwealth Coatings*, and it does not conflict with a decision of any other court. The holding requested by petitioner – that incomplete disclosure *alone* requires a court to vacate an arbitration award, even where the facts, if revealed, would not demonstrate an arbitrator's "evident partiality" – finds no support in the text of FAA § 10(a)(2) or in any judicial decision construing it.

II. Even if petitioner had presented an issue warranting this Court's plenary review, this case would be a poor vehicle for deciding it. The issue presented arises in a highly unusual factual posture not likely to recur and from an arbitration that proceeded not pursuant to an explicit agreement or arbitration organization's procedures, but rather through *ad hoc* decisions made between the parties. Moreover, petitioner asks this Court to grant review of a case from an interlocutory decision, which is contrary to the Court's longstanding policy against piecemeal appeals. Petitioner itself predicts that the proceedings on remand from the decision below will generate further appeals. Petitioner thus does not present an issue of general importance warranting this Court's review.

I. THE DECISION BELOW IS CORRECT AND CREATES NO CONFLICT WITH THE DECISIONS OF THIS OR ANY OTHER COURT

FAA § 10(a)(2) provides that the district court "may make an order vacating" an arbitration award "where there was evident partiality . . . in the arbitrators, or either of them." 9 U.S.C. § 10(a)(2). All American seeks vacatur of the arbitration award in this case even though it concedes that "the facts to be disclosed would not result in the arbitrator's disqualification." Pet. 13. The petition thus proceeds entirely on the premise that a failure of "disclosure" (Pet. 9) constitutes a substantive violation of

§ 10(a)(2)'s "evident partiality" standard.[6] There is no basis in the text of the FAA, this Court's decisions, or the decisions of any other court for that extraordinary proposition.

A. The Seventh Circuit's Decision Is Consistent With § 10(a)(2)

By its plain terms, § 10(a)(2) authorizes a district court to vacate an arbitration award upon a showing of "evident partiality . . . in the arbitrators, or either of them." Petitioner purports to derive two principles from that text: (1) that the "evident partiality" of both party-appointed and neutral arbitrators must be assessed in precisely the same way, Pet. 10; and (2) that, even absent a showing of "evident partiality," a party-appointed arbitrator's incomplete disclosure requires a district court to vacate the arbitration award. The text of § 10(a)(2), however, cannot bear the heavy weight imposed by petitioner.

1. Petitioner acknowledges that § 10(a)(2) makes no facial distinction between neutral and party-appointed arbitrators, but it draws precisely the wrong conclusion from that textual silence. Rather than mandate vacatur of the award, § 10(a)(2)'s silence on any distinctions to be drawn between neutral and party-appointed arbitrators must be construed in light of the agreement reached by the parties to arbitrate their dispute. As this Court has explained, "the FAA's proarbitration policy does not operate without regard to the wishes of the contracting parties." *Mastrobuono v. Shearson Lehman Hutton, Inc.*,

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[6] Petitioner's brief to the court of appeals likewise claimed: "The question here is *not* whether Mr. Jacks's prior attorney-client relationship with Sphere Drake would have, if disclosed, provided All American with a valid basis to disqualify him from serving (as presumed by Sphere Drake); rather, the question is whether Mr. Jacks's failure to provide full and candid disclosure in order to conceal his prior attorney-client relationship from All American and the other arbitrators constitutes evident partiality requiring vacatur of the award pursuant to § 10(a)(2) of the FAA." All American 7th Cir. Br. at 14, No. 02-2458.

514 U.S. 52, 57 (1995). "Just as they may limit by contract the issues which they will arbitrate, . . . so too may they specify by contract the rules under which that arbitration will be conducted." *Volt Info. Sciences, Inc. v. Board of Trustees*, 489 U.S. 468, 479 (1989) (holding that parties could agree to incorporate state procedural law that the FAA might otherwise preempt).

Accordingly, § 10(a)(2) must be interpreted and applied in light of the parties' specific arbitration agreement. When All American launched the arbitration that gave rise to this litigation, it announced the appointment of a party arbitrator and invited Sphere Drake to name its own party arbitrator in its response to the demand for arbitration. *See* All American 7th Cir. Br. at 6 ("In its notice demanding arbitration, All American designated Robert Mangino as its party-appointed arbitrator and requested that Sphere Drake appoint an arbitrator."). That arbitration demand did not invoke any particular procedural rules, but rather proceeded on an *ad hoc* basis.

All American clearly understood that its arbitration agreement with Sphere Drake provided for party-appointed arbitrators who would *not* be "neutral" (and therefore "impartial") in the same way that the umpire is neutral, for its petition for a writ of certiorari (like its briefs below) repeatedly draws a distinction between "neutral arbitrators and party-appointed arbitrators." Pet. 11; *see also, e.g.*, Pet. i-ii, 3, 9-10, 16-17. Indeed, petitioner relies heavily on precedent specifically "recognizing that party selected arbitrators are not expected to be 'neutral.'" Pet. 15 (citing *Metropolitan Prop. & Cas. Ins. Co. v. J.C. Penney Cas. Ins. Co.*, 780 F. Supp. 885, 890-93 (D. Conn. 1991)).

All American's advocacy of a standard that each party-appointed arbitrator be as neutral and impartial as the umpire is thus fatally undermined by the very arbitration agreement that it concededly entered with Sphere Drake. As Judge Learned Hand explained long ago:

> Arbitration may or may not be a desirable substitute for trials in courts; as to that the parties must decide in each instance. But when they have adopted it, they must be content with its informalities; they may not hedge it about with those procedural limitations which it is precisely its purpose to avoid. They must content themselves with looser approximations to the enforcement of their rights than those that the law accords them, when they resort to its machinery.

American Almond Prods. Co. v. Consolidated Pecan Sales Co., 144 F.2d 448, 451 (2d Cir. 1944). *See also Aetna Cas. & Sur. Co. v. Grabbert*, 590 A.2d 88, 93 (R.I. 1993) ("[T]he parties would not consider the appointment of an arbitrator a valued right to be bargained for and litigated over if they contemplated no more than the appointment of a neutral arbitrator."); *Astoria Med. Group v. Health Ins. Plan of Greater New York*, 227 N.Y.S.2d 401, 405 (N.Y. 1962) ("The right to appoint one's own arbitrator, which is of the essence of tripartite arbitration . . . , would be of little moment were it to comprehend solely the choice of a 'neutral.' It becomes a valued right . . . only if it involves a choice of one believed to be sympathetic to his position or favorably disposed to him.").

Buttressing this conclusion is the fact that the agreement here allowed *ex parte* contacts between the parties and their respective arbitrators through the end of discovery, which further belies any suggestion that the party-appointed arbitrators were expected to act as neutrals. *See Nationwide Mut. Ins. Co. v. First State Ins. Co.*, 213 F. Supp. 2d 10, 18 (D. Mass. 2002) (permitting *ex parte* contacts makes it "evident that the parties never intended [party-appointed arbitrators] to be neutral to the same extent as the Umpire"). Moreover, the parties evinced an understanding that even the *umpire* need not meet the impartiality standards for federal judges, for they allowed him to serve despite his disclosure that he owned stock in a company that recently had made a bid to acquire All American. *See* Pet. App. 6a ("A judge can't hold even a

single share of a party's stock, but this would not imply 'evident partiality' for purposes of § 10(a)(2)."). "Parties are free to choose for themselves to what lengths they will go in quest of impartiality. Section 10(a)(2) just states the presumptive rule, subject to variation by mutual consent." *Id.* at 4a. *See also Commonwealth Coatings*, 393 U.S. at 151 (White, J., concurring) (noting that parties may agree to waive circumstances that would be grounds for vacatur under the evident partiality standard).[7]

2. Even if § 10(a)(2) somehow could be construed to require the same standard for "evident partiality" to be applied to neutral umpires and party-appointed arbitrators, petitioner has no textual basis for its assertion that § 10(a)(2) requires a court to vacate an arbitration award for an arbitrator's failure to make a disclosure to the parties where the requisite "evident partiality" is not otherwise satisfied. As one court has explained, § 10(a)(2)

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[7] Congress designed the Act "to make arbitration agreements as enforceable as other contracts, but not more so." *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 n.12 (1967). "Thus, as with any other contract, the parties' intentions control." *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985). The FAA's "primary substantive provision," 9 U.S.C. § 2, states that arbitration agreements "'shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.'" *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24-25 (1991). Section 4 requires that the "arbitration proceed in the manner provided for in [the parties'] agreement." 9 U.S. C. § 4. And § 5 specifically requires that the method for selecting arbitrators contained in the parties' agreement "shall be followed." *Id.* § 5. *See, e.g., Cargill Rice, Inc. v. Empresa Nicaraguense Dealimentos Basicos*, 25 F.3d 223, 225 (4th Cir. 1994) ("parties may determine by contract the method under which arbitrators for their disputes will be appointed") (citing cases); *ATSA of California, Inc. v. Continental Ins. Co.*, 754 F.2d 1394, 1395 (9th Cir. 1985) ("Under 9 U.S.C. § 5, the parties' method of appointing arbitrators must be followed. Generally, partisan arbitrators are permissible."). The legislative history to the FAA is just as plain as the statute: "Arbitration agreements are purely matters of contract, and the effect of the bill is simply to make the contracting party live up to his agreement. . . . An arbitration agreement is placed upon the same footing as other contracts, where it belongs." H.R. Rep. No. 68-96, at 1 (1924).

"makes no mention of an arbitrator's failure to disclose information as a basis for vacating an arbitration award." *ANR Coal Co. v. Cogentrix of North Carolina, Inc.*, 173 F.3d 493, 497 (4th Cir. 1999).

Petitioner seeks (at 16) to capitalize on the court of appeals' statement that, after the cessation of permissible *ex parte* contacts, the party-arbitrators "are supposed thereafter to be impartial adjudicators" pursuant to ARIAS-U.S. rules. Pet. App. 5a. Even assuming that the parties had agreed to arbitrate by ARIAS-U.S. rules (which they did not[8]), all that the court of appeals could possibly have meant by this statement was that party-appointed arbitrators have a duty to hear the evidence fairly, even though they may be predisposed to their party's position.[9] But the court clearly did not mean that Arbitrator Jacks was expected to behave as a neutral, and petitioner

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[8] Petitioner's carefully worded statement (at 16) that "the Seventh Circuit found the parties' arbitration had been conducted" "under [the] auspices" of the AIDA Reinsurance and Insurance Arbitration Society ("ARIAS-U.S.") is misleading because it attempts to capitalize on a mistake in the court of appeals' recitation of the facts of this case. All American has never claimed that the parties agreed to arbitrate pursuant to ARIAS-U.S. rules (its factual statement here is likewise devoid of any such claim), and nothing in the record supports that suggestion. Indeed, All American's only reference to the ARIAS-U.S. rules below was to support its arguments that Jacks, as a founding member of ARIAS-U.S., was aware of the importance of disclosure. *See* All American 7th Cir. Br. at 26. *See also* Pet. 6 n.8. As All American recognizes, the district court noted the same fact, but it did not hold or even suggest that the parties agreed to be bound by ARIAS-U.S. rules. *See* Pet. 16 n.4 (citing Pet. App. 15a). Moreover, in its court of appeals brief, All American claimed only that the reinsurance "slips" evidencing the alleged contracts provided, in full: "Arbitration Clause" or "Arbitration Clause – Law and Jurisdiction Illinois, USA." All American 7th Cir. Br. at 6 n.8. All American never argued that this language required arbitration under ARIAS-U.S. (or any other organization's) rules.

[9] Canon II of the ARIAS-U.S. Code of Conduct provides that "[a]rbitrators shall conduct the dispute resolution process in a fair manner and shall serve only in those matters in which they can render a just decision." ARIAS-U.S. Code of Conduct, Canon II, *available at* http://www.arias-us.org/code_canon02.shtml.

identifies nothing in the record to suggest as much. *See id.* at 3a ("in the main party-appointed arbitrators are *supposed* to be advocates"). Indeed, even the district court – which vacated the award – clearly understood that "Jacks was a party-appointed, as opposed to a neutral, arbitrator." *Id.* at 26a n.8; *id.* (distinguishing "cases concern[ing] alleged partiality on the part of the neutral arbitrator, or concern[ing] alleged partiality of panels composed entirely of purportedly neutral arbitrators"). All American could have insisted that the arbitrators all be neutral, but it did not.

B. The Decision Below Properly Interpreted *Commonwealth Coatings*

Petitioner's contention that the Seventh Circuit's judgment conflicts with this Court's decision in *Commonwealth Coatings* has no merit. Indeed, the decision below is perfectly consistent with this Court's decisions.

1. In *Commonwealth Coatings*, this Court vacated an arbitration award where the undisclosed information by the neutral arbitrator showed his evident partiality. There, the "neutral in a tripartite arbitration was engaged in *ongoing* business relations with one of the parties, 'and the relationship even went so far as to include the rendering of services on the very projects involved in this lawsuit.' " Pet. App. 10a (quoting *Commonwealth Coatings*, 393 U.S. at 146 (plurality opinion)).

Justice Black's plurality opinion relied on *Tumey v. Ohio*, 273 U.S. 510 (1927), which had reversed a conviction, pursuant to the Due Process Clause, based on the judge's disqualifying pecuniary interest in the specific case before him. *Commonwealth Coatings*, 393 U.S. at 148. Justice White's concurring opinion likewise focused on whether an arbitrator would be "disqualified by a business relationship with the parties." *Id.* at 150. This Court has subsequently characterized *Commonwealth Coatings* (along with *Tumey*) as a case "in which the

adjudicator has a pecuniary interest in the outcome." *Withrow v. Larkin*, 421 U.S. 35, 47 & n.14 (1975).[10]

Petitioner concedes that Arbitrator Jacks did not meet that standard of ongoing pecuniary interest. *See* Pet. 13 (framing the issue as when "the facts to be disclosed would not result in the arbitrator's disqualification"). Nor could All American reasonably argue otherwise. Jacks had no pecuniary interest in Sphere Drake, he had ceased practicing law with Mayer, Brown & Platt four years prior to becoming an arbitrator in this matter, his representtations of a Sphere Drake subsidiary during the years when he was engaged in the practice of law were insufficient to warrant disqualification, and the ownership and management of the Sphere Drake entities that he had represented had turned over completely since his representations.

2. Petitioner unpersuasively attempts to morph *Commonwealth Coatings* into a decision requiring vacatur of an arbitration award when an arbitrator simply fails to disclose information, even when that information concededly would not demonstrate evident partiality. *See* Pet. 12 n.3 (contending that *Commonwealth Coatings* adopted a "*per se* prophylactic disclosure rule"). The court below

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[10] Although the plurality in *Commonwealth Coatings* used broad language in deeming even " 'the slightest pecuniary interest' on the part of the judge" to require vacatur of the arbitration award before it, 393 U.S. at 148 (quoting *Tumey*, 273 U.S. at 524), the Court later held that this passage was both "dicta" and "a misreading of *Tumey*." *Aetna Life Ins. Co. v. Lavoie*, 475 U.S. 813, 825 n.3 (1986). Instead, the Court explained that *Tumey* should be read to require vacatur only when the judge's interest in the case before the court is " 'direct, personal, substantial, and pecuniary.' " *Id.* at 825-26 (quoting *Tumey*, 273 U.S. at 523) (internal brackets omitted). Given this Court's subsequent reading of that passage in *Commonwealth Coatings*, there is no merit to petitioner's suggestion that *Commonwealth Coatings* established an independent disclosure standard divorced from the crucial issue of whether disqualification would have been required because of the "evident partiality" of the arbitrator. *Cf. Metropolitan Stevedore Co. v. Rambo*, 515 U.S. 291, 300 (1995) ("Breath spent repeating dicta does not infuse it with life.").

properly rejected that characterization of *Commonwealth Coatings*. *See* Pet. App. 10a.

Although Justice White's concurring opinion encouraged an "atmosphere of frankness at the outset," *Commonwealth Coatings*, 393 U.S. at 151 (White, J., concurring), that exhortation was aimed at encouraging "voluntary compliance with the decree, without need for judicial enforcement," so that the parties might waive an "evident partiality" challenge even where the disclosed facts might require disqualification on that basis. *Id.* (Noting that the parties themselves are the best "judge[s] of the arbitrator's impartiality. That role is best consigned to the parties, who are the architects of their own arbitration process, and are far better informed of the prevailing ethical standards and reputations within their business.").

As the decision below recognizes, the "point of *Commonwealth Coatings* is that the sort of financial entanglements that would disqualify a judge will cause problems for a neutral under § 10(a)(2) unless disclosure is made and the parties' consent obtained." Pet. App. 10a ("being on one side's payroll is a form of partiality condemned by § 10(a)(2)"). All American itself concedes that the undisclosed information about Jacks' prior representation of Sphere Drake and its subsidiary would not have, if disclosed, demonstrated evident partiality or required disqualification. Pet. 13. Under a proper reading of *Commonwealth Coatings*, "[t]he material and relevant facts an arbitrator fails to disclose may demonstrate his 'evident partiality' under 9 U.S.C. § 10(a)(2). However, nondisclosure, even of such facts, has no independent legal significance and does not in itself constitute grounds for vacating an award." *ANR Coal*, 173 F.3d at 499.[11]

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[11] Petitioner claims to find a "circuit split" on a question – whether the plurality opinion or concurring opinion in *Commonwealth Coatings* is more authoritative – that is not relevant to the issue presented in the petition. Pet. 8 n.2. Indeed, petitioner does not ask the Court to grant review to resolve that supposed "split" or otherwise assert that this Court's clarification of the distinctions between those opinions in

C. The Circuits Are Not In Conflict On This Issue

Petitioner does not claim that the decision below conflicts with that of any other court of appeals, and it does not dispute the court of appeals' observation about the unprecedented nature of the district court's decision – "the first time since the Federal Arbitration Act was enacted in 1925 that a federal court has set aside an award because a party-appointed arbitrator on a tripartite panel, as opposed to a neutral, displayed 'evident partiality.'" Pet. App. 3a. Instead, petitioner asserts conflicts with only one federal district court decision and two state court decisions purportedly "applying the disclosure requirement of *Commonwealth Coatings* to all arbitrators – including party-appointed arbitrators." Pet. 14. Even those cases, however, are inapposite.

1. In *Metropolitan Property*, the district court found "overt misconduct" due to a party-appointed arbitrator's undisclosed *ex parte* contacts. 780 F. Supp. at 893. But it is undisputed in this case that All American and Sphere Drake specifically agreed to permit such contacts. *See* p.5, *supra*. Moreover, the district court in *Metropolitan Property* did *not* base its holding solely on the lack of disclosure, but rather on a substantive breach of the parties' agreement to arbitrate. 780 F. Supp. at 893 ("that

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Commonwealth Coatings would benefit All American in any way. As we explain in the text above, petitioner's position finds no support in either the plurality or the concurrence in *Commonwealth Coatings*, and the decision below was correct no matter which opinion is deemed controlling. In any event, the holdings of the other court of appeals cases cited by petitioner (*id.*) are inapposite to the issue petitioner has presented to this Court. *See, e.g., University Commons-Urbana, Ltd. v. Universal Constructors Inc.*, 304 F.3d 1331, 1342-43 (11th Cir. 2002) (remanding for fact-findings on possible evident partiality where district court had engaged in no fact-finding); *Schmitz v. Zilveti*, 20 F.3d 1043, 1049 (9th Cir. 1994) (holding that National Association of Securities Dealers Code required arbitrator in securities case "to make a reasonable effort to inform himself of his firm's representation of" parent company); *Merit Ins. Co. v. Leatherby Ins. Co.*, 714 F.2d 673, 683 (7th Cir. 1983) (reversing district court judgment vacating arbitration award absent "evidence of actual or probable partiality or corruption").

agreement contains no provisions whatsoever that could be construed as even remotely sanctioning the type of *ex parte* activity alleged here"); *cf. Sunkist Soft Drinks, Inc. v. Sunkist Growers, Inc.*, 10 F.3d 753, 759 (11th Cir. 1993) (finding *ex parte* contacts between a party and its appointed arbitrator "not only unobjectionable, but commonplace").[12]

In *Barcon Associates, Inc. v. Tri-County Asphalt Corp.*, 430 A.2d 214, 220 (N.J. 1981) – which involved only state law and not the FAA – the arbitrator was owed substantial sums of money from ongoing business dealings with the party that appointed him.[13] That was precisely the type of financial interest absent in this case. In the other state court case (a two-page decision), the arbitrator was an officer or director of two corporations that had performed substantial work in the two previous years for the party appointing him. *Northwest Mech., Inc. v. Public Utils. Comm'n*, 283 N.W.2d 522, 523 (Minn. 1979).[14] Thus, those cases involved direct and continuing financial interests of a type that is absent here.

By contrast, petitioner has "failed to cite a single [court of appeals] case holding that a failure to disclose . . . constitutes an independent basis for vacatur absent proof that, in addition, the nondisclosure proves one of the statutory grounds for vacatur." *ANR Coal*, 173 F.3d at 499-500.

2. Moreover, the decisions of the courts of appeals uniformly confirm the common expectation that "party-

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[12] In any case, an asserted conflict between decisions of a court of appeals and a district court is no reason to grant certiorari. *See* Robert L. Stern *et al.*, *Supreme Court Practice* § 4.8, at 237-40 (8th ed. 2002).

[13] The court inexplicably "reject[ed] the notion . . . that the parties' contract should prevail" with regard to the duties of party-appointed arbitrators. 430 A.2d at 219 (4-3 decision).

[14] *Florasynth, Inc. v. Pickholz*, 750 F.2d 171, 173 (2d Cir. 1984), cited by petitioner (at 14), is also inapposite, as that case was decided on statute of limitations grounds, not "evident partiality."

designated arbitrators are not neutral, each being biased in favor of the party that designated him." *United Transp. Union v. Gateway W. Ry.*, 284 F.3d 710, 714 (7th Cir. 2002); *see also id.* at 711 ("since the party members of the panel are expected to vote in accordance with their principals' wishes (though they don't always do so), it is the neutral who is the real 'judge' and usually decides the case"); *Sunkist*, 10 F.3d at 760 ("a party-appointed arbitrator is permitted, and should be expected, to be predisposed toward the nominating party's case"). *Cf. Delta Mine Holding Co. v. AFC Coal Props., Inc.*, 280 F.3d 815, 821 (8th Cir. 2001) (holding that arbitration agreement providing for tripartite panel "expressly contemplated the selection of partial arbitrators"), *cert. denied*, 123 S. Ct. 87 (2002).[15] To be sure, a party-appointed arbitrator should act fairly and in good faith. "[O]utright chicanery" is not sanctioned, *Commonwealth Coatings*, 393 U.S. at 150 (White, J., concurring), only the customary predisposition that the parties have bargained for in agreeing to tripartite arbitration.

The courts of appeals have likewise consistently applied an "onerous standard for vacatur" that All American could not possibly meet: "[t]he alleged partiality must be direct, definite, and capable of demonstration rather than remote, uncertain, or speculative." *Al-Harbi v. Citibank, N.A.*, 85 F.3d 680, 683 (D.C. Cir. 1996) (internal quotation marks omitted).[16] Because arbitration "is customized, not

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[15] Earlier this Term, this Court denied a petition for a writ of certiorari in *Delta Mine*, which also presented the question, as framed by All American here, whether a party-appointed arbitrator has the same disclosure obligations as a neutral under *Commonwealth Coatings*. *Cf. South Park Ind. Sch. Dist. v. United States*, 453 U.S. 1301, 1303-04 (1981) (Powell, Circuit Justice) (denying stay where "[t]he issues presented by applicants are almost identical to those presented three years ago, when the Court voted to deny certiorari").

[16] *See also Peoples Sec. Life Ins. Co. v. Monumental Life Ins. Co.*, 991 F.2d 141, 146 (4th Cir. 1993) (same); *Health Servs. Mgmt. Corp. v. Hughes*, 975 F.2d 1253, 1264 (7th Cir. 1992) (same); *Sheet Metal Workers Int'l Ass'n Local Union No. 420 v. Kinney Air Conditioning Co.*, 756

off-the-rack, dispute resolution," *IDS Life Ins. Co. v. Royal Alliance Assocs., Inc.*, 266 F.3d 645, 651 (7th Cir. 2002), petitioner cannot demonstrate that, in the particular circumstances presented here, any other court would have applied § 10(a)(2) to vacate the arbitration award in favor of Sphere Drake. Absent such a showing of clear conflict among the courts of appeals, further review by this Court is unwarranted.

D. Petitioner's Selectively Invoked Arbitration Rules And Policy Arguments Are Misplaced And Without Merit

1. Petitioner invokes certain arbitration rules, but nowhere demonstrates that such rules were part of the parties' agreement to arbitrate. First, petitioner recites (at 16) the preamble to the ARIAS-U.S Code of Conduct for the proposition that party-appointed arbitrators should adhere to the same disclosure standards as the neutral.[17] But even if that language had been incorporated into the parties' agreement to arbitrate – and it was not – the antecedent paragraph explicitly provides that "[n]othing in these Guidelines is intended to or should be deemed to establish new or additional grounds for judicial review of arbitration appointments or arbitration awards nor establish any substantive legal duty on the part of arbitrators." ARIAS-U.S. Code of Conduct, Introduction, *available at* http://www.arias-us.org/code_intro.shtml. There would

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F.2d 742, 745-46 (9th Cir. 1985) ("The party alleging evident partiality must establish specific facts which indicate improper motives on the part of the Board. The appearance of impropriety, standing alone, is insufficient."); *International Produce, Inc. v. A/S Rosshavet*, 638 F.2d 548, 551 (2d Cir. 1981) (holding "appearance of partiality" insufficient); *Andros Compania Maritima, S.A. v. Marc Rich & Co.*, 579 F.2d 691, 700 (2d Cir. 1978) ("[W]e have not been quick to set aside the results of an arbitration because of an arbitrator's alleged failure to disclose information.").

[17] As explained in note 8, *supra*, the court below mistakenly suggested that ARIAS-U.S. rules governed the arbitration at issue in this case. Petitioner does not seriously contend here that those rules applied.

thus be no basis for a court to vacate the arbitration award based on any putative violation of an ARIAS-U.S. disclosure standard. Petitioner also relies (at 17) on Canon IV of the ARIAS-U.S. Code of Conduct, without demonstrating that the exclusive withdrawal standards specifically provided there have been satisfied in this case.[18]

Second, petitioner relies (at 17-18) on a proposed – and thus unenacted – revision to the American Bar Association's ("ABA") Code of Ethics for Arbitrators. Since its adoption in 1977, that Code has provided that non-neutral arbitrators "need not include as detailed information as is expected from persons appointed as neutral arbitrators." ABA Code of Ethics for Arbitrators in Commercial Disputes, Canon VII(B)(1), *available at* http://www.adr.org/index2.1.jsp?JSPssid=15718&JSPsrc=upload\LIVESITE\Rules_Procedures\Ethics_Standards\code.html. Moreover, the proposed disclosure revision championed by petitioner would retain the current provision that "[n]on-neutral arbitrators are not obliged to withdraw if requested to do so by the party who did not appoint them." *Id.*, Canon VII(B)(2); *see* Code of Ethics for Arbitrators in Commercial Disputes (Proposed Revision 2000), 671 PLI/Lit 1039, *1055-*1056 (proposed Canon IX(C)). Other commonly used arbitration rules likewise offer no support for petitioner's general position.[19]

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[18] Comment 2 to Canon IV requires withdrawal only when (1) "all parties" request withdrawal; (2) the arbitrator determines that he or she should withdraw; (3) "procedures agreed upon by the parties for resolving challenges to arbitrators have been followed and require withdrawal"; or (4) "required by the contract or law." *See* http://www.arias-us.org/code_canon04.shtml. The first two reasons are obviously inapplicable because neither all parties nor Jacks himself determined that withdrawal was appropriate, and petitioner cannot point to any procedures established by the parties or to a contract provision or law that might invoke the latter two grounds.

[19] The Commercial Arbitration Rules of the American Arbitration Association ("AAA") provide that, "[u]nless the parties agree otherwise, an arbitrator selected unilaterally by one party is a party-appointed

Finally, even if any of the foregoing rules could somehow be imputed to the parties' agreement to arbitrate, such arbitration rules and ethical guidelines "do not give a federal court license to vacate an award on grounds other than those set forth in 9 U.S.C. § 10." *ANR Coal*, 173 F.3d at 499; *see also id.* at 500 ("[M]ere nondisclosure does not in itself justify vacatur."); *Merit*, 714 F.2d at 680 ("[E]ven if the failure to disclose was a material violation of the ethical standards applicable to arbitration proceedings, it does not follow that the arbitration award may be nullified judicially."). Thus, the court below was fully correct in reversing the district court's judgment vacating the arbitration award because Arbitrator Jacks' evident partiality cannot be established.

2. Petitioner claims (at 19-25) that good policy requires the Court to establish a disclosure requirement independent of – and far more demanding than – § 10(a)(2)'s "evident partiality" standard. In making that argument, petitioner repeatedly takes liberties with the record in claiming that Jacks' nondisclosure was "intentionally . . . misleading," "intentionally deceptive," or "intentionally . . . false and misleading." Pet. 23-25. The only support in the record for those over-blown characterizations was the overturned district court's description of Jacks' "inadequate disclosure" as "'negligent or even intentional.'" Pet. 6 (quoting Pet. App. 30a). In making that statement, however, the district court did not make a formal finding

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arbitrator and is not subject to disqualification pursuant to [Rule] 19." AAA Commercial Arbitration Rule 12(b), *available at* http://www.adr.org (Rules, Commercial Dispute Resolution Procedures); *see also id.*, Rule 19 (providing for disqualification only of neutral arbitrator); *cf. Delta Mine*, 280 F.3d at 822 n.4 (Rule 12 "provide[s] that, absent an agreement to the contrary, party-appointed arbitrators are presumed to be non-neutral."); ABA Code of Ethics for Arbitrators in Commercial Disputes, Canon VII ("In [tripartite] arbitrations, the two party-appointed arbitrators should be considered nonneutrals unless both parties inform the arbitrators that all three arbitrators are to be neutral or unless the contract, the applicable arbitration rules, or any governing law requires that all three arbitrators be neutral.").

that Jacks' nondisclosure actually *was* intentional. In fact, no hearing was held at which Jacks' intent could have been determined. In view of the court of appeals' conclusion – uncontested here – that Jacks' nondisclosure would not have disqualified him as a federal judge sitting in this case, it is hard to see how even such an allegedly "intentional" omission could be deemed material in context.

Petitioner instead asserts that a party arbitrator's disclosure obligations should go "beyond that required by a judge presiding over a lawsuit." Pet. 13. Elsewhere, however, petitioner candidly "acknowledge[s] that arbitrators cannot, and should not, be expected to be as impartial as judges." Pet. 23. But, if arbitrators (even neutrals) are not expected to be as impartial as judges, then it makes no sense for a court to impose a greater obligation of disclosure on arbitrators. Petitioner defends its extravagant theory on the ground that "[c]ommon sense suggests that an umpire would want to know that a party arbitrator had a sustained and significant attorney-client relationship with the appointing party in assessing his position and potential bias during deliberations." Pet. 13. Of course, federal judges – whom petitioner concedes are expected to be more impartial than arbitrators – regularly sit on multi-judge panels, yet petitioner fails to explain why they might be less concerned about their colleagues' past activities than an arbitrator.

In any case, the court of appeals correctly held that "we have not been given any reason to think that [U]mpire Huggins wanted more information from Jacks in order to know what to make of [his] arguments during the panel's deliberations." Pet. App. 11a. All American – whose burden it was to show evident partiality[20] – simply failed to

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[20] *See, e.g., Al-Harbi*, 85 F.3d at 683 ("We agree with the Fourth Circuit that 'the burden on a claimant for vacation of an arbitration award due to "evident partiality" is heavy, and the claimant must establish *specific facts* that indicate improper motives on the part of an

carry that burden. That fact-bound determination does not warrant this Court's review. Moreover, as a policy matter, "[t]he approach proposed by [petitioner] would permit a disgruntled party to seize upon an undisclosed relationship as a pretext for invalidating the award. Under such a rule, an arbitration award could be vacated due to an arbitrator's failure to disclose a trivial fact even though that fact, if known prior to the arbitration, would not have enabled the losing party to have the arbitrator removed for cause. Such a system would undermine the parties[] faith in commercial arbitration and make the task of finding qualified arbitrators exceedingly burdensome." *ANR Coal*, 173 F.3d at 500 (internal quotation marks and citations omitted).

II. THE DECISION BELOW IS AN ESPECIALLY POOR VEHICLE FOR DECIDING THE CIRCUMSTANCES IN WHICH ALLEGED ARBITRATOR BIAS REQUIRES VACATUR OF AN AWARD

Even if petitioner had presented an issue meriting review, this case would be a poor vehicle for deciding it. First, the issue presented arises in a highly unusual factual posture not likely to recur. In demanding arbitration, All American merely announced the appointment of its party arbitrator and then asked Sphere Drake to appoint its party arbitrator. *See* p.13, *supra*. Thus the arbitration demand did not invoke any particular procedural rules, but rather proceeded on an *ad hoc* basis. To resolve this case, therefore, the Court would have to discern the parties' intent in a highly unusual situation that is unlikely to be replicated.

Second, petitioner seeks immediate review of an interlocutory judgment that, by its own admission, could well become moot. This case is now on remand to the district court, where petitioner has renewed three arguments for

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arbitrator.' ") (quoting *Peoples Security Life Ins.*, 991 F.2d at 146); *Health Servs. Mgmt.*, 975 F.2d at 1258 n.3.

vacating the arbitration award that neither the district court nor the Seventh Circuit has yet addressed.

Shortly after the court below denied petitioner's rehearing en banc petition, petitioner asked the district court to stay all remand proceedings concerning the three "other independent grounds raised by All American in support of vacating the award," pending this Court's disposition of its petition for certiorari. All American Motion To Stay Pending Application for Certiorari at 1, Civil Action No. 01 C 5226 (N.D. Ill. filed Nov. 12, 2002).[21] Petitioner contended that a stay was warranted to avoid "prejudicing All American's rights to obtain Supreme Court review." *Id.* at 2. As petitioner noted, "[s]hould the [district court] again vacate the award (a decision which would be subject to review by the Seventh Circuit)," then Supreme Court review of the evident-partiality issue presented here "may be jeopardized on mootness grounds." *Id.*[22]

Given that the issue presented in its petition for a writ of certiorari may possibly become moot as a result of those remand proceedings presently pending and being briefed in the district court, petitioner presents no reason why this Court should depart from its normal practice of declining to review judgments on interlocutory matters. The interlocutory character of this case "alone furnishe[s] sufficient ground for the denial" of the petition. *Hamilton-Brown Shoe Co. v. Wolf Bros. & Co.*, 240 U.S. 251, 258 (1916); *see also Brotherhood of Locomotive Firemen v. Bangor & Aroostook R.R.*, 389 U.S. 327, 328 (1967) (per curiam) ("[B]ecause the Court of Appeals remanded the case, it is not yet ripe for review by this Court."); *Virginia*

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[21] In addition to the "evident partiality" question in its petition here, All American claimed before the district court "(2) that the hearing denied All American fundamental fairness; (3) that the panel members exceeded their authority; and (4) that the panel exhibited a manifest disregard of the law." Pet. App. 12a-13a.

[22] All American did not appeal the district court's denial of its stay motion and has stipulated to a schedule by which briefing on all remaining issues will be completed by March 28, 2003. *See* App., *infra*, 6a.

Military Inst. v. United States, 508 U.S. 946, 946 (1993) (Scalia, J., respecting the denial of the petition for writ of certiorari) ("We generally await final judgment in the lower courts before exercising our certiorari jurisdiction.").

Granting review now will neither obviate a remand nor eliminate the prospect of future requests for this Court's review, either on the present issue or those to be decided on remand. *See Hamilton-Brown Shoe*, 240 U.S. at 258 ("[E]xcept in extraordinary cases, the writ is not issued until final decree."); *cf. Major League Baseball Players Ass'n v. Garvey*, 532 U.S. 504, 508 n.1 (2001) (per curiam) ("[W]e have authority to consider questions determined in earlier stages of the litigation where certiorari is sought from the most recent of the judgments of the Court of Appeals."). Accordingly, All American can offer no compelling reason to grant its petition.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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Counsel for Respondent

March 7, 2003

APPENDIX

APPENDIX A

$4 Million XS $1 Million

451 SCR

Registration No. AH 0095097 Page of

REINSURED: ALL AMERICAN LIFE INSURANCE COMPANY, CHICAGO ILLINOIS, (NAIC CODE 60097) AS UNDERWRITTEN FOR BY WEB MANAGEMENT LLC.

PERIOD: Losses occurring in respect of risks attaching during the 12 month period commencing 1st June 1997.

TYPE: EXCESS OF LOSS REINSURANCE.

CLASS: In respect of all business classified by the Reinsured as Personal Accident business including but not limited to Accidental Death and Dismemberment, Occupational Accident, Occupational Accident Carveout, Accidental Death Carveout and Catastrophe covers and/or as original.

TERRITORY: Losses wheresoever occurring.

LIMITS: US$4,000,000 any one occurrence.
EXCESS OF:
US$1,000,000 any one occurrence.

REINSTATEMENT: Four Reinstatements each at 100% Additional Premium..

PREMIUM: Minimum and Deposit Premium US$400,000.

Payable as follows:-

10% at 1st June 1997
20% at 1st August 1997
30% at 1st November 1997
40% at 1st February 1998

Adjustable annually at 3.75% of the applicable Net Premium Income accruing in respect of risks attaching during the period hereon.

First adjustment at 31st May 1998
Final adjustment at 31st May 2000

DEDUCTIONS: 15% brokerage
(plus 1% F.E.T. as applicable).

WARRANTY: Two Life Warranty.

EXCLUSIONS:
i) Employers Liability
ii) Professional Sports
iii) Medical Business
iv) London Market Excess of Loss Business howsoever written.
v) Aviation and Marine Bodily Injury
vi) Group Life
vii) Credit Cards
viii) Airport Ticket and Coupon Business

LOSS RESERVE: Funding of outstanding losses by Letter of Credit if required.

US
CLASSIFICATION: US Reinsurance Treaty.

2a

EIUA10324

BEST AVAILABLE COPY

GENERAL CONDITIONS:

War and Civil War Exclusion - NMA 464
Ultimate Net Loss Clause
Service of Suit Clause USA NMA 1998
E.C.O. Inclusion Clause
Errors and Omissions Clause
Insolvency Clause
Insolvency Fund Exclusion Clause
Arbitration Clause
Offset Clause
Access to Books and Records
Definition of occurrence - occurrence means any one accident or series of accidents arising out of one event.
Interlocking Clause.
Intermediary Clause - John B. Collins Associates Inc.
Several Liability Notice (Reinsurance) LSW 1001.

WORDING: To be agreed Leading Underwriter only.

INFORMATION:

1. Reinsured's applicable estimated net premium income for the purpose of this reinsurance: US$10,000,000 (in respect of risks attaching during the period 12 months commencing 1st June 1997).

2. Information titled 'WEB Management LLC' seen and noted by Reinsurers hereon.

3. Net lines protected hereunder

   US$ 1,000,000 any one person
   US$10,000,000 any one programme

4. Occupational Accident business is protected with a Per Risk Program excess of US$30,000 which inures to the benefit of this Reinsurance or so deemed.

3a

SCHEDULE B REGISTRATION NO. AU00990937

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SCR

100%

100 %

John Hancock Mutual Life Ins Co
Per
JE+ Printed Name
P2114597

17.5% CHIYODA EUROPE

K 9 9 2 6 9 X 9 7		
C1401	LISBEA	NCAD

WHL. NKORLE 1/10/97.
Wtd. Prem Paid (Ccy) by 1/11/97
and received by 15/11/97.

15:11:97 O

10%
TO SIGN

ACCEPTED UNDER CONTRACT
No 50413
Per SPHERE DRAKE INS CO
970610NXX10A

Subject to written confirmation

EIUA16326

PAGE 4 of 4

4a

Confirmation of Acceptance under Horace Holman Contract No: 50413 underwritten by Sphere Drake Insurance Plc per Sphere Drake Underwriting Management Ltd.

Declaration No: 970610NXX10A

Insured/Reinsured: ALLAMERICAN LIFE / WOS MANAGEMENT

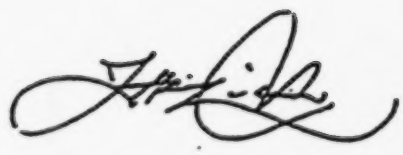
Inception Date: 1.6.97

Sum Insured/Original Limit: $ 4,000,000 x $ 1,000,000

Written Line 10% TO SIGN

Acceptance Date 3.10.97

Producing Broker SCB



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EIUA10327

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS

Civil Action No. 01C 5226

SPHERE DRAKE INSURANCE LIMITED,
Plaintiff,

v.

ALL AMERICAN LIFE INSURANCE COMPANY,
Defendant.

[January 28, 2003]

ORDER

It is hereby ordered that All American Life Insurance's ("All American") renewed motion to vacate the arbitration award shall be presented as follows:

1. All American shall have until February 19, 2003 to file its brief in support of its renewed motion to vacate the arbitration award;

2. Sphere Drake Insurance Limited shall have until March 12, 2003 to file its brief in opposition to All American's renewed motion to vacate the arbitration award;

3. All American shall have until March 28, 2003 to file its reply in further support of its renewed motion to vacate the arbitration award.

ENTERED:

/s/ REBECCA R. PALLMEYER
Judge Rebecca R. Pallmeyer

Supreme Court, U.S.
FILED
MAR 18 2003
OFFICE OF THE CLERK

(3)

No. 02-1168

IN THE
Supreme Court of the United States

AMERICAN GENERAL LIFE INSURANCE COMPANY,

Petitioner,

v.

SPHERE DRAKE INSURANCE LIMITED,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

REPLY BRIEF

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15 pp

STATEMENT PURSUANT TO RULE 29.6

Petitioner American General Life Insurance Company Rule 29.6 Statement was set forth at page (iii) of the Petition, and there are no amendments to that Statement.

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INTRODUCTION

Section 10 of the Federal Arbitration Act ("FAA") authorizes a district court to vacate an arbitration award where there was "evident partiality or corruption in the arbitrators, *or either of them*." 9 U.S.C. § 10(a)(2) (emphasis added). In the present case, the district court found that the intentional failure of Sphere Drake's party-appointed arbitrator to disclose his significant prior attorney-client relationship with Sphere Drake demonstrated evident partiality. The fact that there was a non-trivial business relationship between Sphere Drake's party arbitrator and Sphere Drake *combined* with the fact that the arbitrator purposefully concealed that relationship amply supports the district court's finding of evident partiality under § 10(a)(2).

The Seventh Circuit circumvents the disclosure rule announced in *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145 (1968), by reasoning that party-appointed arbitrators are mere shills, exempt from any disclosure obligation and free to exhibit evident partiality. Such a distorted interpretation is not supported by § 10(a)(2), which by its plain language prohibits evident partiality in both party-appointed arbitrators and "neutral" arbitrators. Moreover, *Commonwealth Coatings* and its progeny leave no doubt that the requirement to disclose any non-trivial relationship applies to all members of a tripartite arbitration panel. Finally, the parties here expressly intended the party-appointed arbitrators to be more than mere pitchmen. At the outset of the proceedings, the parties explicitly agreed that all members of the panel should disclose any prior relationships with the parties and their law firms. Such disclosure benefited not only the parties, but also the neutral arbitrator, who needed to assess any potential bias on the part of his fellow arbitrators. The Seventh Circuit's decision exempting the party arbitrators from § 10(a)(2) cannot be squared with its finding that the parties intended that the party arbitrators be "impartial adjudicators." Pet. App. 5a.

This case is an appropriate vehicle for this Court to reaffirm that the prophylactic disclosure rule announced in *Commonwealth Coatings* applies to all arbitrators, whether party-appointed or neutral. Reaffirming the need for full and candid disclosure by all arbitrators will help promote arbitration as a legitimate and desirable alternative to litigation. The Seventh Circuit's decision sanctioning evident partiality on the part of an "impartial adjudicator" impugns the integrity of the arbitral process and should not be allowed to stand.

ARGUMENT

POINT I

SPHERE DRAKE IGNORES THE PLAIN LANGUAGE OF § 10(a)(2)

Sphere Drake argues that All American's petition "proceeds entirely on the premise that a failure of 'disclosure' constitutes" a violation of § 10(a)(2)'s evident partiality standard. Br. in Opp. 11-12. Sphere Drake's characterization of All American's argument is wrong. This case is not one in which a party-appointed arbitrator simply failed to disclose a prior non-trivial relationship with the appointing party. Sphere Drake's party arbitrator deceived All American and the other arbitrators by failing to disclose his significant prior attorney-client relationship at the outset of the proceedings, thereby demonstrating his evident partiality.

The Seventh Circuit held that the statutory ground for vacating an arbitration award under § 10(a)(2) of the FAA does not extend to party-appointed arbitrators. As demonstrated in All American's Petition, the Seventh Circuit's holding is inconsistent with the plain language of § 10(a)(2), which authorizes a district court to vacate an award where there was "evident partiality or corruption in the arbitrators, *or either of them*." *See* Pet. 10 (emphasis added). The italicized words leave no room to dispute the intent of Congress to include party arbitrators on a tripartite panel.

Sphere Drake attempts to rehabilitate the Seventh Circuit's unprecedented decision by arguing that the plain language of § 10(a)(2) should be construed "in light of the parties' specific agreement to arbitrate." Br. in Opp. 13. According to Sphere Drake, because the parties appointed their arbitrators, All American could not expect them to be "neutral" or "impartial," presumably meaning there was an intent to exempt them from the prohibition of § 10(a)(2) against evident partiality. Sphere Drake's argument is without factual or legal support.

First, the parties held an organizational meeting at which each panel member made a disclosure concerning his current and past relationships with the parties, their respective law firms and the other panel members in accordance with the procedure agreed to among the panel and counsel. Logically, the parties would not have bothered to go through the process of soliciting disclosures from the party-appointed arbitrators unless the parties believed those disclosures would be meaningful, *i.e.*, would provide a basis for assessing potential bias or evident partiality.

Second, disclosure by Sphere Drake's party-appointed arbitrator served a number of salutary purposes. Had Sphere Drake's party arbitrator disclosed the truth about his extensive attorney-client relationship with Sphere Drake, All American would have had a meaningful opportunity to exercise its right to challenge his appointment. *See Metropolitan Prop. & Cas. Ins. Co. v. J.C. Penney Cas. Ins. Co.*, 780 F. Supp. 885, 894 (D. Conn. 1991) (a party-appointed arbitrator can be disqualified prior to arbitration); *Lipschutz v. Gutwirth*, 304 N.Y. 58, 65 (N.Y. 1952) (same). Moreover, such disclosure would have provided the umpire with information necessary to assess the appropriate weight to be given to the party-appointed arbitrator's views. Commentators recognize the importance of such disclosure: "[w]hat the neutral learns about the party arbitrators' relationships with their parties should also be useful to him in evaluating the points those arbitrators make to him about the case." Stephen C. Rogers, *Can Tripartite Arbitration Panels*

Reach Fair Results?, 8 No. 1 Disp. Resol. Mag. 27, 29 (Fall 2001). *See also* the Revised Uniform Arbitration Act § 12, Comment 5:

> The integrity of the process demands that the non-neutral arbitrators chosen by the parties, like neutral arbitrators, disclose pertinent interests and relationships to all parties as well as other members of the arbitration panel. *It is particularly important for the neutral arbitrator to know the interest of the arbitrator selected by each of the parties if, for example, such non-neutral arbitrator is being paid on a contingent-fee basis.*

Emphasis added.

Finally, strict disclosure standards are a necessary check on the significant power exercised by arbitrators. The Seventh Circuit was wrong to hold that arbitrators should be held to a less stringent disclosure standard than judges. Instead, as this Court recognized in *Commonwealth Coatings*, "we should, if anything, be even more scrupulous to safeguard the impartiality of arbitrators than judges, since the former have completely free rein to decide the law as well as the facts and are not subject to appellate review." 393 U.S. at 149. Rigorous disclosure standards are also necessary for arbitrators because, as the Seventh Circuit acknowledged, industry arbitration "often uses panels composed of industry insiders, the better to understand the trade's norms of doing business and the consequences of proposed lines of decision." App. at 4a. This reality demands that the parties and other arbitrators be cognizant of the extent of an arbitrator's relationship to the party that selected him or her, which can only be achieved through the full and candid disclosure by all arbitrators, as required by this Court in *Commonwealth Coatings*.

POINT II

THE SEVENTH CIRCUIT'S DECISION IS CONTRARY TO *COMMONWEALTH COATINGS*

The Seventh Circuit held here that the disclosure requirement set forth in *Commonwealth Coatings* applies only to a neutral arbitrator in a tripartite arbitration, and not to party-appointed arbitrators. This holding is unsupportable. *Commonwealth Coatings*, which involved precisely the same type of tripartite panel as the present case, draws no distinction between the disclosure obligations of neutral and party-appointed arbitrators. *See Commonwealth Coatings*, 393 U.S. at 151-52 (White, J., concurring) (encouraging an "atmosphere of frankness at the outset," which could not be achieved where only one of three arbitrators on a tripartite panel is required to disclose his or her prior relationships); *id.* at 149 (Black, J., concurring) ("[w]e can perceive no way in which the effectiveness of the arbitration process will be hampered by the simple requirement that *arbitrators* disclose to the parties any dealings that might create an impression of possible bias") (emphasis added). *See also Standard Tankers (Bahamas) Company, Ltd. v. Motor Tank Vessel, Akti*, 438 F. Supp. 153, 159 (E.D.N.C. 1977) (*Commonwealth Coatings* "placed a disclosure burden on arbitrators appointed by the parties or otherwise."); Pet. 10-15 (authorities cited therein).

Sphere Drake attempts to shore up the Seventh Circuit's holding by suggesting that *Commonwealth Coatings* is in fact a disqualification case, rather than a disclosure case. Br. in Opp. 18 (stating that, in *Commonwealth Coatings*, the Justices "focused" on whether an arbitrator would be disqualified by a business relationship with the parties). Having thus misinterpreted the holding of *Commonwealth Coatings*, Sphere Drake explains that the true issue in the present case is whether or not Sphere Drake's party arbitrator had an "ongoing pecuniary interest" in the outcome of the arbitration. *Id.* This is wrong. *Commonwealth Coatings*, which represents the seminal case

concerning an arbitrator's — any arbitrator's — duty to disclose, holds that the failure of an arbitrator to disclose a non-trivial business relationship with a party constitutes evident partiality under the FAA, regardless of whether the arbitrator had an "ongoing pecuniary interest." Indeed, in *Commonwealth Coatings*, there had been no dealings between the arbitrator in question and the respondent for "*about a year* immediately preceding the arbitration." 393 U.S. at 146 (emphasis added).

Applying the *Commonwealth Coatings* holding to the present case, the district court found that Sphere Drake's arbitrator was evidently partial due to his failure to disclose a significant four-year attorney-client relationship with Sphere Drake, a relationship misleadingly described by the arbitrator as simply providing "limited corporate advice." All American has never argued, contrary to Sphere Drake's suggestion, that the party arbitrator's nondisclosure itself constitutes an "independent" ground for vacating the award. Br. in Opp. 19. Rather, All American argued, and the district court agreed, that given the totality of the circumstances, the arbitrator's "troublesome" and "disappointing" failure to disclose his "substantial" relationship with Sphere Drake was sufficient to establish evident partiality under § 10(a)(2). Pet. App. 27a; 13a. Importantly, the Seventh Circuit did not disagree with this finding. Instead, the Seventh Circuit wrongly held that Sphere Drake's party arbitrator was exempt from § 10(a)(2) and any duty to disclose, and thus *Commonwealth Coatings* did not apply.

Sphere Drake erroneously argues that a failure to disclose is never sufficient to establish evident partiality. Br. in Opp. 19. However, the very case to which respondent cites in support of this position, *ANR Coal Company, Inc. v. Cogentrix of N. Carolina, Inc.*, 173 F.3d 493, 500 (4th Cir. 1999), itself holds that "an arbitrator's failure to reveal facts may be relevant in determining evident partiality under 9 U.S.C. § 10(a)(2)." The fact that the court in *ANR Coal* held that the failure of a neutral arbitrator to disclose prior representation by his law firm

of a party, *with which the arbitrator had no personal involvement*, did not demonstrate evident partiality is irrelevant; here, the trial court found that the arbitrator's failure to disclose his own substantial attorney-client relationship with Sphere Drake did constitute evident partiality.

Finally, All American does not concede, as alleged by Sphere Drake, that the undisclosed information about the arbitrator's prior relationship would not have, if disclosed, required disqualification. Br. in Opp. 19. All American has not taken any position on that question because it is simply not relevant to this case.[1] The arbitrator's intentional concealment of his prior, non-trivial relationship is an integral part of the fact pattern; it cannot be ignored in an effort to change the issue in this case from evident partiality to disqualification.

The Supreme Court Rules explicitly provide that a grant of certiorari is appropriate where "a state court or a United States court of appeals . . . *has decided an important federal question in a way that conflicts with relevant decisions of this Court.*" Sup. Ct. R. 10 (emphasis added). Here, the Seventh Circuit has disregarded this Court's ruling in *Commonwealth Coatings* that all arbitrators must disclose any non-trivial business relationship with a party to the arbitration under § 10(a)(2). Such a blatant departure from this Court's prior holding demands the Court's review. Thus, respondent's contention that a grant of certiorari is not warranted because there is no circuit split is simply irrelevant.

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1. Throughout its brief, Sphere Drake contends that All American "concedes" that the prior relationship, if disclosed, would not have required disqualification or demonstrated evident partiality. Br. in Opp. 11, 19 (citing to Pet. 13). All American has made no such concession. Sphere Drake misconstrues All American's Petition, which states merely that the Seventh Circuit's misguided interpretation of *Commonwealth Coatings* "stems, at least in part from the court's implicit finding that disclosure by a party arbitrator serves no salutary purpose if the facts to be disclosed would not result in the arbitrator's disqualification." Pet. 13.

POINT III

ARBITRATION RULES AND POLICY ARGUMENTS UNDERMINE THE SEVENTH CIRCUIT'S DECISION

The Seventh Circuit's decision is broadly worded and, if permitted to stand, will be used to excuse (and indeed encourage) the practice of misleading disclosures by party-appointed arbitrators in a variety of circumstances. Hence, respondent is incorrect to argue that All American's reliance upon arbitration rules and policy arguments is "misplaced and without merit." Br. in Opp. 23-27. In fact, arbitration rules and policy arguments vividly illustrate the negative impact the Seventh Circuit's decision will have on the integrity of the arbitration process.

First, the Seventh Circuit operated under the assumption that the ARIAS-U.S. rules were employed, and thus its decision must be read as applicable to any case where those rules, or similar rules, are in effect. Pet. 16, 19 (finding that the "arbitration was conducted under the auspices of . . . ARIAS-US" and that according to the relevant rules, the party-appointed arbitrators are supposed to be "impartial adjudicators."). Having determined that Sphere Drake's party arbitrator was expected to be an *impartial adjudicator*, the Seventh Circuit nevertheless held that he had no disclosure obligation. Thus, the court's holding eviscerates any disclosure obligation for a party-appointed arbitrator regardless of the parties' expectation that the party arbitrators would be impartial and provide full disclosure, even where the applicable rules *require* disclosure. This decision squarely conflicts with the intended purpose of the disclosure rules adopted by various arbitration institutions, including the American Bar Association Revised Code of Ethics. *See Code of Ethics for Arbitrators in Commercial Disputes (Proposed Revision 2000)*, 671 PLI/Lit 1039, * 1056 (March 2002).

Second, this Court has adopted a clear policy of encouraging parties to resolve their disputes through arbitration, rather than litigation. Pet. 19-22. Failing to require full and honest disclosure

from all arbitrators will frustrate this stated policy by undermining the public's confidence in arbitration as a fair and viable alternative to litigation. *See Barcon Assoc., Inc. v. Tri-County Asphalt Corp.*, 430 A.2d 214, 219-20 (N.J. 1981) ("[A] party-designated arbitrator . . . must remain faithful to the obligation which rests upon him to maintain 'broad public confidence in the integrity and fairness of the (arbitration) process.'") (citing to the First Code of Ethics for Arbitrators in Commercial Disputes jointly drafted by the American Arbitration Association and the American Bar Association); *Metropolitan Prop. & Cas. Ins. Co. v. J.C. Penney Cas. Ins. Co.*, 780 F. Supp. 885, 893 (D. Conn. 1991) ("even a party-appointed arbitrator in the tripartite context 'has a responsibility not only to the parties but also to the process itself, and must observe high standards of conduct so that the integrity and fairness of the process will be preserved.'").

POINT IV

THIS CASE IS AN APPROPRIATE VEHICLE FOR REAFFIRMING *COMMONWEALTH COATINGS*

Sphere Drake's argument that this case is an inappropriate vehicle for Supreme Court review because the arbitral procedure was *ad hoc* is a red herring aimed at diverting the Court's attention from the real issue. Whether the arbitral procedure was *ad hoc* or institutional is irrelevant. Both types of arbitrations are governed by the FAA. The issue is whether Sphere Drake's party-appointed arbitrator was evidently partial in violation § 10(a)(2) of the FAA.

Further, Sphere Drake argues that this case is not ripe for certiorari review because the Seventh Circuit remanded the case for further proceedings in the district court. However, it is black letter law that this Court is not constrained by the final judgment rule. *See* 28 U.S.C.A. § 1254(1) (the Court may review cases by "writ of certiorari granted upon the petition of any party to any civil or criminal case, before or after rendition of judgment or decree."). Indeed, in *Forsyth v. Hammond*, 166 U.S. 506,

513 (1897), this Court referred to certiorari as "a comprehensive and unlimited power" that may be utilized "irrespective of any ruling or determination" of the court of appeals. This Court has exercised its jurisdiction in a wide range of cases requiring further action below. *See, e.g.*, *School Bd. of Nassau Cty., Fla. v. Airline*, 480 U.S. 273 (1987) (granting review after court of appeals reversed district court's dismissal and remanded for further proceedings); *INS v. Cardoza-Fonseca*, 480 U.S. 421 (1987) (granting review after court of appeals remanded case to Board of Immigration Appeals for further proceedings); *Stafford v. Briggs*, 444 U.S. 527 (1980) (granting review after court of appeals issued order upholding personal jurisdiction and remanding to district court for trial); *accord* C. Wright & A. Miller, 17 Fed. Prac. & Proc. Juris. 2d § 4036, at 3 ("In a wide range of cases, certiorari has been granted after a court of appeals has disposed of an appeal from a final judgment on terms that require further action in the district court, so that there is no longer any final judgment."). This case is ripe for review.

CONCLUSION

Petitioner respectfully submits that the Court should grant a writ of certiorari to reaffirm that the disclosure rule announced in *Commonwealth Coatings* applies to all arbitrators, neutral and party-appointed.

Respectfully submitted,

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